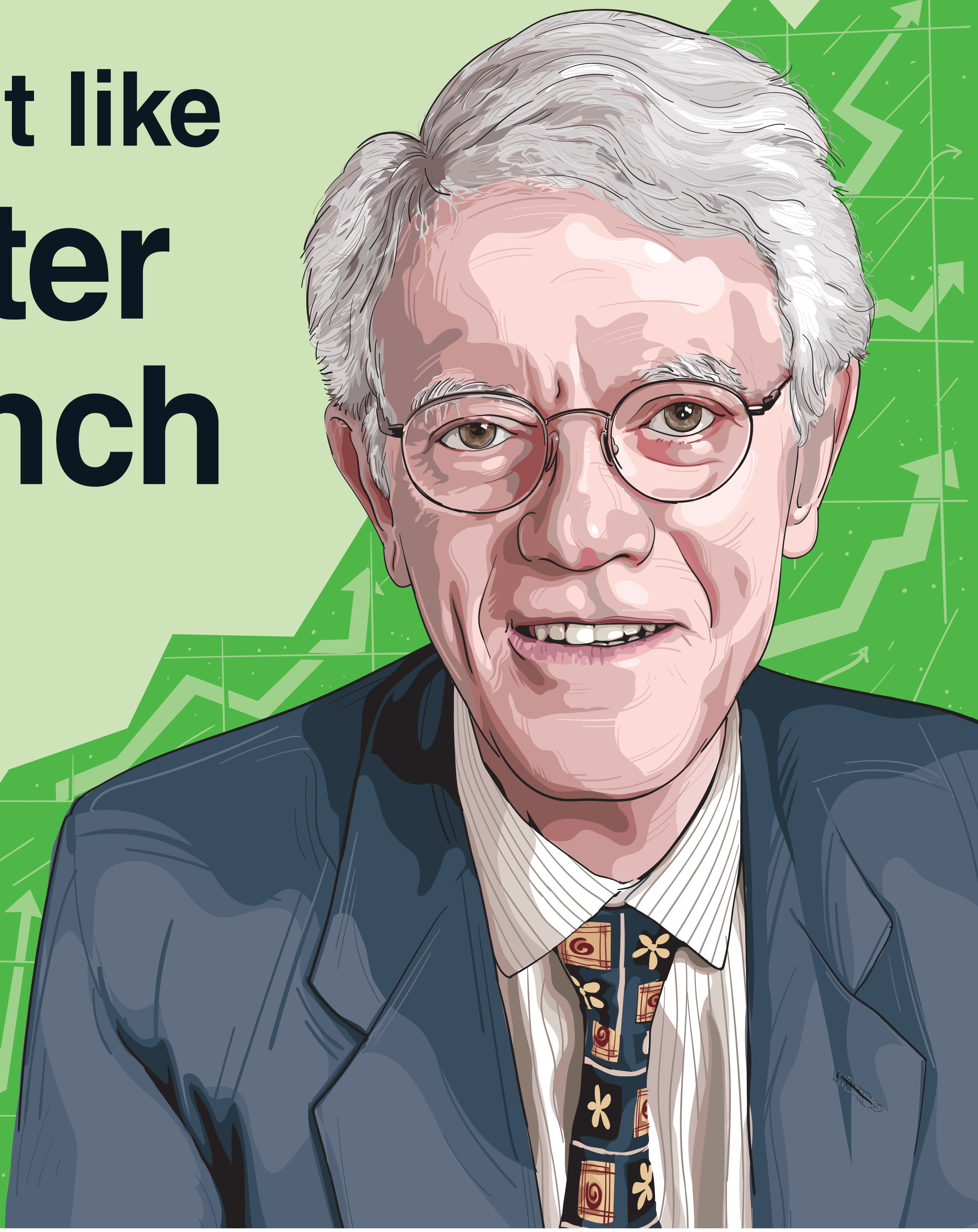
Value Research

Wealth Insight

August 2024 ₹125

Ideas for savvy stock investors

Profit like Peter Lynch



27 Passive funds for stock investors

Analyst's Diary 28
Can this power player's bet on green energy pay off?

Analyst's Diary 34
Are we in a stock market bubble? Find out

HDFC MUTUAL FUND
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HDFC Manufacturing Fund An open-ended equity scheme following manufacturing theme	• To generate long-term capital appreciation • Investment predominantly in equity & equity related securities of companies engaged in the manufacturing theme	 Investors understand that their principal will be at very high risk
HDFC Infrastructure Fund An open ended equity scheme following infrastructure theme	• To generate long-term capital appreciation / income • Investment predominantly in equity and equity related securities of companies engaged in or expected to benefit from the growth and development of infrastructure	

*Investors should consult their financial advisers, if in doubt about whether the product is suitable for them.

For latest Riskometer, investors may refer to the Monthly Portfolios disclosed on the website of the Fund viz. www.hdfcfund.com

The Scheme(s) being thematic in nature carries higher risks versus diversified equity mutual funds on account of concentration and theme specific risks.

MUTUAL FUND INVESTMENTS ARE SUBJECT TO MARKET RISKS, READ ALL SCHEME RELATED DOCUMENTS CAREFULLY.

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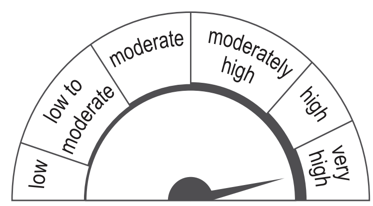
ICICI Prudential Business Cycle Fund (An open ended equity scheme following business cycles based investing theme) is suitable for investors who are seeking*:	
• Long term wealth creation • An equity scheme that invests in Indian markets with focus on riding business cycles through dynamic allocation between various sectors and stocks at different stages of business cycles.	 Investors understand that their principal will be at Very High risk
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The Risk-o-meter(s) specified above will be evaluated and updated on a monthly basis.
Please refer www.icicipruamc.com/news-and-updates/all-news for more details on scheme riskometers.

Mutual Fund investments are subject to market risks, read all scheme related documents carefully.

Value Research
Wealth Insight
August 2024
Volume XVIII, Number 2

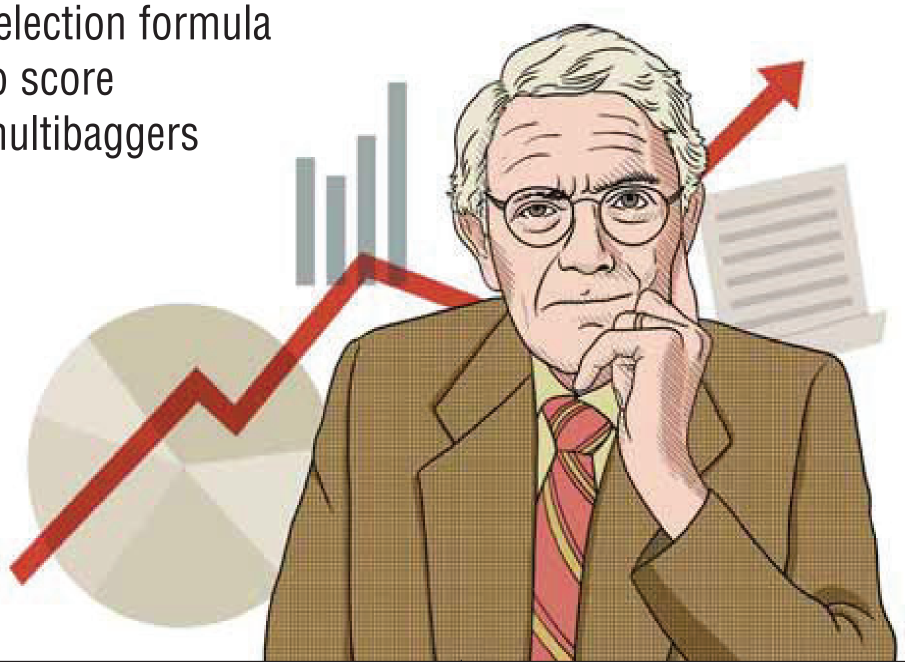
EDITORIAL POLICY

The goal of Wealth Insight, as with all publications from Value Research, is not just limited to generating profitable ideas for its readers; but to also help them in generating a few of their own. We aim to bring independent, unbiased and meticulously-researched stories that will help you in taking better-informed investment decisions, encouraging you to indulge in a bit of research on your own as well.

All our stories are backed by quantitative data. To this, we add rigorous qualitative research obtained by speaking to a wide variety of stakeholders. We firmly stick to our belief of fundamental research and value-oriented approach as the best way to earn wealth in the stock market. Equally important to us is our unwaveringly focus on long term planning.

Simplicity is the hallmark of our style. Our writing style is simple and so is the presentation of ideas, but that should not be construed to mean that we over-simplify.

Read, learn and earn – and let's grow and evolve as we undertake this voyage together.



Contents

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by Dhirendra Kumar

How to be one up

Peter Lynch's timeless investment wisdom in the modern era

Popular investing trends come and go like seasons, but in all that churn, some figures stand out like monuments. Peter Lynch, the legendary fund manager who turned Fidelity's Magellan Fund into a powerhouse, is one such luminary. His approach to investing wasn't just effective—it was revolutionary in its simplicity and accessibility. Lynch's mantra, "Invest in what you know," resonates as strongly today as it did when he first uttered those words. In an era of complex algorithms and high-frequency trading, his down-to-earth philosophy serves as a refreshing reminder that the best investment ideas might be hiding in plain sight in our everyday experiences and observations.

Decades ago, when I was fresh out of college and had not even started a career, I found a copy of Peter Lynch's 'One Up on Wall Street'. Looking back at the evolution of my ideas about investments, I realise that this was a seminal moment in my life. If this sounds like hyperbole to you, remember that compared to today, information and ideas were scarce resources before the internet. To have access to great ideas was a real differentiator. Moreover, because the mind was not cluttered with the stream of useless factoids that the online world throws at one today, these ideas had the space to take root and flourish. I devoured the Lynch book when I got it, and then over the next few months, read and re-read it. In today's info-clutter, I might have flipped through it, read its Wikipedia page, and decided that that was enough.

Lynch's wisdom was like a beacon in the fog of financial jargon and intimidating market analysis. He demystified the process of stock selection, encouraging readers to look beyond the numbers and see the stories behind companies. His approach was refreshingly democratic–you didn't need a finance MBA or be a professional to be a successful investor. You just needed to be observant, curious, and willing to do your homework.

At the time when I read it, One Up on Wall Street was just two to three years old. Lynch was actually known only for his incredible track record as a fund manager. From 1977 to 1990, while managing the Fidelity Magellan Fund in the US, he generated an annualised return of 29.4 per cent, making it the best-performing fund in the world. However, now the nature of his legacy has changed. While that investment performance made Lynch a legend in the world of investments, it is his writings on equity investing that have firmly secured his legacy.

Our cover story this month delves deep into Lynch's book and the investment styles that he describes. Not only do we explain his investment concepts, but our team has also applied his framework to the Indian equity markets. I'm sure some of you will think this to be a bit too old school in today's fast-paced, tech-driven market. However, we believe that Lynch's principles are more relevant than ever. In an age of information overload and hyperactive trading, his emphasis on understanding businesses and spotting opportunities in your own backyard offers a grounding perspective. Moreover, his approach encourages investors to think long-term and resist the temptation of short-term market noise–which is a skill far more valuable than any information about the markets or stock-selection techniques.

Our cover story is a great read, but I recommend that you see it only as an appetiser. In a magazine, we have space to barely scratch the surface of Lynch's wisdom. His books are treasure troves of investment wisdom that every investor should read.

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Why Follow

Aveek Mitra is a seasoned long-term investor with 27 years of experience in the financial sector. As the founder of Aveksat Financial Advisory, he offers both portfolio and equity advisory services. In addition to providing insights on market and industry trends, he consistently advises investors on strategies to safeguard their investments. Prior to establishing his own firm, Mitra garnered extensive experience working with several esteemed organisations, including L&T and Usha Martin.

The investment safety advocate

Next valuation metric for Defence, Renewable, Small Cap make blockbuster debut!!
Market Cap / Total Global Addressable Market by 2047 😌
For Defence / Renewable / Small Cap

All around I see more of marketing pitches to gather clients, increase AUM, increase fee or commission income than a genuine concern for client well being, safety and growth of his capital.
If you check performance records than media blitzkrieg by big names, you may understand the reality.Anyone writing / talking / making videos on investment analysis is good. It helps many non finance or not CA or non MBAs in knowing what to look & what to avoid in investment decisions. But if it's all that's making investors successful over a long period then all finance professors would have been very rich by now!
Kindly note unless you have seen multiple cycles, went through crests & troughs of emotional upheaval, faced failures, handled big success with poise & humility, it's tough to be an advisor / fund manager who can aim to help others.

Big 3 IT firms headcount down by 64000. And poor growth anticipated for the sector. It is combination many factor:
1) Excess recruitment in Covid period
2) Some low end jobs are getting redundant with advancement of technology.
3) Very little innovation from big Indian IT companies. They focussed more on productivity gain & undercutting each other.
4) Big IT spenders in the US / EU are still hesitant to budget big IT spends fearing recession & fast technological change.

Tough time for fresh engineering graduates as new jobs are few, salaries are abysmal, job content is poor.
US rate cuts may marginally improve the scenario (new start ups or already struggling ones may get some funding, big companies start spending) but the issue is more structural in nature for big IT services companies.

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Mutual Fund

India's consumption levels surge = Potential investment growth

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Mirae Asset Great Consumer Fund

(An open ended equity scheme following consumption theme.)

Why invest?

- Investment in a long term consumer theme
- Flexibility to invest across market capitalisation & styles

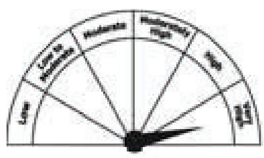
PRODUCT LABELLING

Mirae Asset Great Consumer Fund is suitable for investors who are seeking*

- Long term capital appreciation
- Thematic fund investing in equity & equity related securities of companies benefiting directly or indirectly from consumption led demand in India

*Investors should consult their financial advisors if they are not clear about the suitability of the product.

Scheme Riskometer



Investors understand that their principal will be at Very High Risk

Scheme Benchmark: Nifty India Consumption Index (TRI)
Benchmark Riskometer

The Benchmark is at Very High Risk

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TO KNOW MORE

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Mutual Fund investments are subject to market risks, read all scheme related documents carefully.

Amara Raja inks tech collaboration pact with Gotion High-Tech

Amara Raja Energy & Mobility has signed an agreement with GIB EnergyX Slovakia, a subsidiary of Gotion High-Tech, to licence Gotion's world-class LFP technology for lithium-ion cells. The agreement also provides Amara Raja access to Gotion's cell technology IP and global supply chain network for critical battery materials. Gotion will also provide customer technical support and help Amara Raja establish its gigafactory.

₹31,000 crore

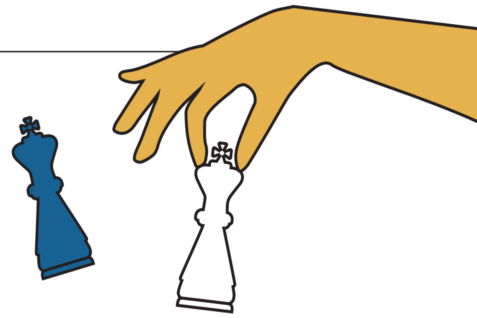
The capex planned by Indian Oil Corp for FY25. This amount would be spent across its various segments, including refining, marketing, pipeline, petrochemicals, alternative energy and city gas distribution.

Adani Group plans a capex of ₹1.3 lakh crore for FY25

The Adani Group plans to nearly double its capital expenditure in FY25 to ₹1.3 lakh crore. Around 70 per cent of this will go towards its green portfolio, including renewable power, green hydrogen and green evacuation. The remaining 30 per cent will be spent on its airports and ports businesses. It plans to raise $2-2.5 billion through equity to fund this capex. Notably, Adani Green Energy has earmarked approximately ₹2 lakh crore to boost its capacity from 10.9 GW to 50 GW by 2030. This strategic move underscores the company's commitment to sustainable growth and infrastructure development.

Dr Reddy's acquires Haleon's Nicotinell products

Dr Reddy's has acquired Haleon's global portfolio (excluding the US) of consumer healthcare brands in the NRT (Nicotine Replacement Therapy) domain for £500 million (around ₹4,550 crore). This acquisition aligns with Dr Reddy's ongoing efforts to increase its presence in the global consumer healthcare market. Haleon's portfolio includes the brand Nicotinell, a global leader in the NRT category, with revenue of around £217 million (around ₹1,976 crore) in 2023.



JSW Infrastructure set to acquire Navkar Corp

JSW Infrastructure has announced its plan to acquire a 70.3 per cent stake in Navkar Corporation at an enterprise value of ₹1,644 crore, marking its foray into the logistics industry. It also plans to acquire an additional 26 per cent stake through an open offer to public shareholders. Navkar operates three container freight stations, an inland container depot and a cargo terminal (Gati Shakti).

UltraTech Cement acquires stake in India Cements

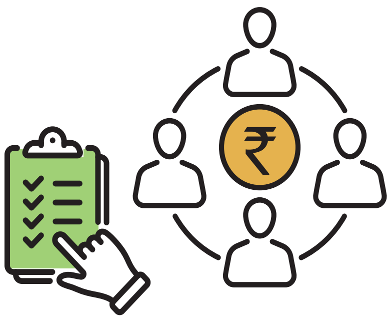
UltraTech Cement, India's largest cement company, acquired a 23 per cent stake in India Cements for ₹1,885 crore. This move is part of the ongoing industry consolidation. Larger players, particularly the Aditya Birla and Adani groups, have made several acquisitions to boost capacity and expand their geographical presence. UltraTech stated it would not control India Cements' operations, and the acquisition is purely a financial investment.

Bajaj Auto launches world's first CNG-powered bike

Bajaj Auto, India's third-largest motorcycle manufacturer, has launched Freedom 125, the world's first CNG-powered two-wheeler, for an ex-showroom price of ₹95,000. The bike, as per the management, has a range of 330 km and carries lower maintenance costs than similar petrol bikes. The company has started accepting limited bookings for the bike in Maharashtra. It plans to launch the model across India by the end of FY25.

Zee shareholders approve a ₹2,000 crore fundraise

Zee plans to raise around ₹2,000 crore through unsecured foreign currency convertible bonds (FCCBs). The bonds carry a coupon of 5 per cent and mature in 10 years. Note that the company was net debt-free as of March 2024. The fundraising approval follows the scrapped plans of the mega-merger between Zee and Sony back in January.

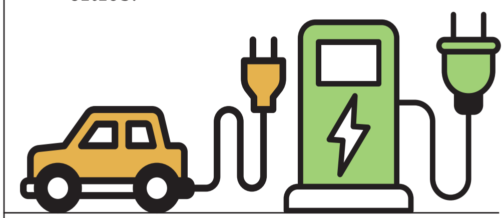


HUL offloads Pureit

HUL plans to sell its two-decade-old water purification business, Pureit, to AO Smith for a consideration of ₹601 crore. The deal will be an all-cash transaction, expected to close by year-end. Pureit generated a revenue of ₹293 crore in FY24, accounting for less than 1 per cent of HUL's revenue. This exit is part of the management's strategic decision to enhance focus on the core products.

BPCL partners with Statiq

BPCL has inked a partnership with Statiq, an EV charging station operator. The partnership is expected to boost the adoption of EVs in India. As per the agreement, the duo will develop an app for BPCL and integrate its existing 2,800 charging stations with Statiq's portfolio. Presently, Statiq operates a vast network of 7,000 charging stations spread across 65 indian cities.



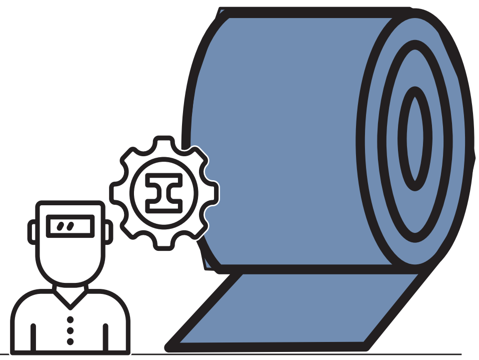
Major results for Q1 FY25

	Revenue	Operating profit	Operating profit margin (bps)	Net profit
Asian Paints	-2.3	-23.8	-4.6	-24.5
Avenue Supermarts	18.6	17.8	0.0	17.5
Bajaj Auto	15.7	23.3	1.2	18.1
HCL Tech	6.7	8.0	0.2	20.5
LTIMindtree	5.1	-5.5	-1.7	-1.5
TCS	5.4	12.3	1.5	8.7

YoY changes

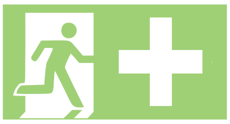
₹30,000 crore

The capex planned by Lloyds Metals & Energy to enhance iron ore mining by 15 MTPA and establish a new steel production facility with a capacity of 4 MTPA by FY29.



₹8,500 crore

The amount Vedanta is raising from its QIP, which will be used for deleveraging and optimising its capital structure. As of FY24, Vedanta had a net debt of ₹56,338 crore.



Glenmark Pharma exits Glenmark Life Sciences

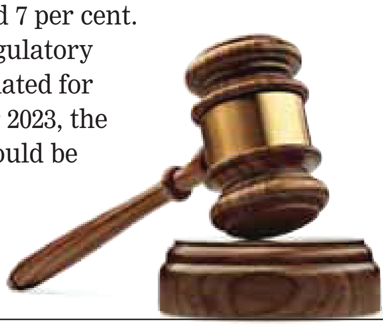
The board of Glenmark Pharma has approved the sale of its remaining 7.8 per cent stake in Glenmark Life Sciences. To recap, Glenmark Pharma sold its 75 per cent stake in Glenmark Life Sciences to the Indian conglomerate Nirma in early 2024. The upcoming stake sale will mark Glenmark Pharma's complete exit from Glenmark Life Sciences.

Tata Group announces a capex plan of ₹30,000 crore

Tata Steel and Tata Power, two powerhouses of the Tata Group, have announced mega capex plans. Tata Steel will invest around ₹10,000 crore annually to increase its total steel production capacity to 40 MTPA by 2030. Likewise, Tata Power plans to incur a capex of ₹20,000 crore in FY25, primarily to expand its renewable energy production capacity.

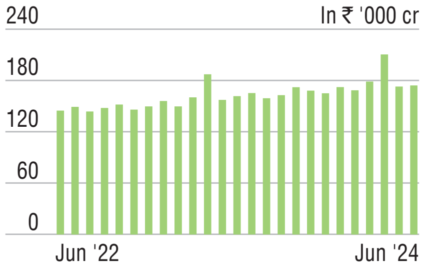
Nazara Tech gets ₹1,120 crore GST notice

Two subsidiaries of Nazara Technologies received GST demand notices of around ₹1,120 crore on July 16, 2024. Following this, Nazara Technologies' share price tanked around 7 per cent. The GST demand notice results from regulatory changes pertaining to how GST is calculated for online gaming companies. In September 2023, the regulatory body announced that GST would be calculated based on the pooled gross bet value instead of gross gaming revenue.

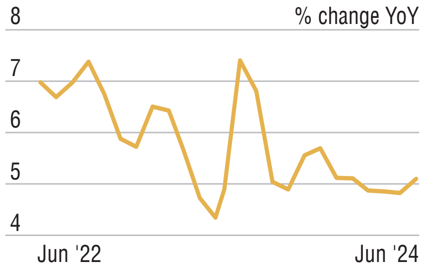


ECONOMIC METRICS

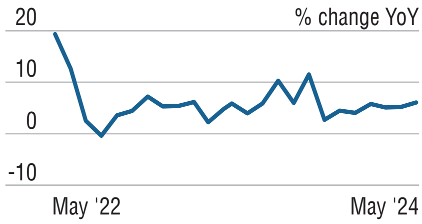
GST collection



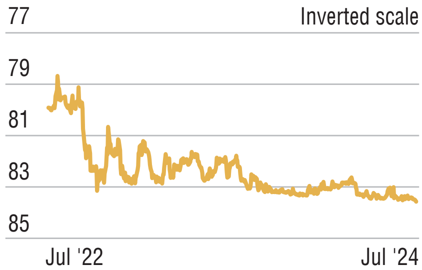
Inflation: Consumer Price Index



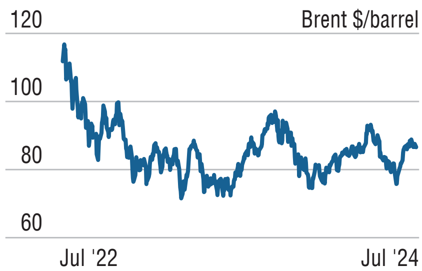
Industrial activity: Index of Industrial Production



₹ vs $



Crude oil



Cementing dominance

Tracking the rise of this cement giant through acquisitions and aggressive capex

UltraTech is the largest cement producer in India. It has achieved this status through years of consistent growth and expansion.

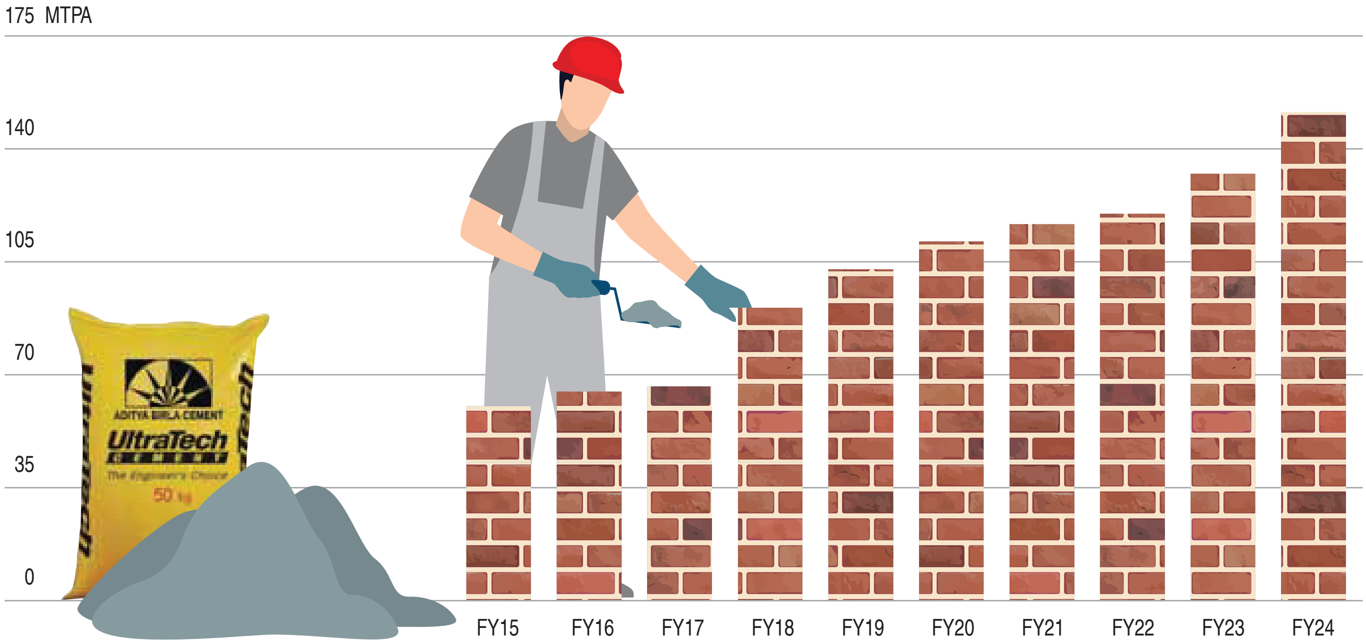
After acquiring the cement business of Kesoram Industries in December 2023, it recently acquired a 23 per cent stake in India Cements for ₹1,889 crore.

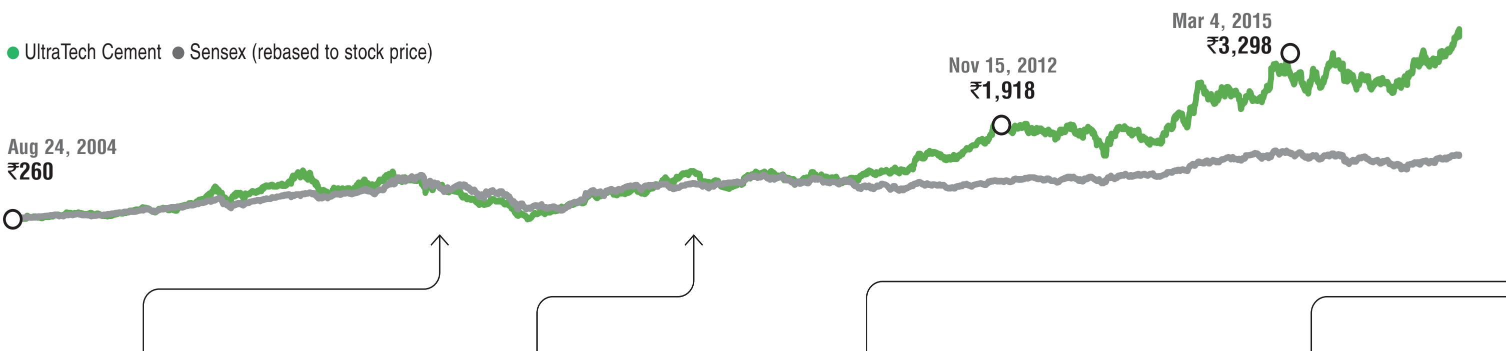
The journey of UltraTech

Part of the diversified Aditya Birla Group, UltraTech's origins date back to the mid-80s when Grasim and Indian Rayon set up the first cement plant. What followed was rapid capacity expansion and business consolidation, with the company reaching a capacity of 8.5 MTPA (million tonnes per annum) by 1998 and subsequently 14.1 MTPA by 2003.

In July 2004, it acquired L&T's demerged cement business for ₹2,200 crore. This acquisition was

Capacity ramp-up over the years





Mar 26, 2008
Commissioned clinker plant of 3.3 MTPA at its unit in Andhra Pradesh.

Apr 29, 2010
Acquired Dubai-based ETA Star Cement.

Jun 29, 2017
Acquired Jaypee Cement with a capacity of 21.1 MTPA at an enterprise value of ₹16,189 crore.

Dec 13, 2018
Acquired Binani Cement under a resolution plan of ₹8,000 crore.

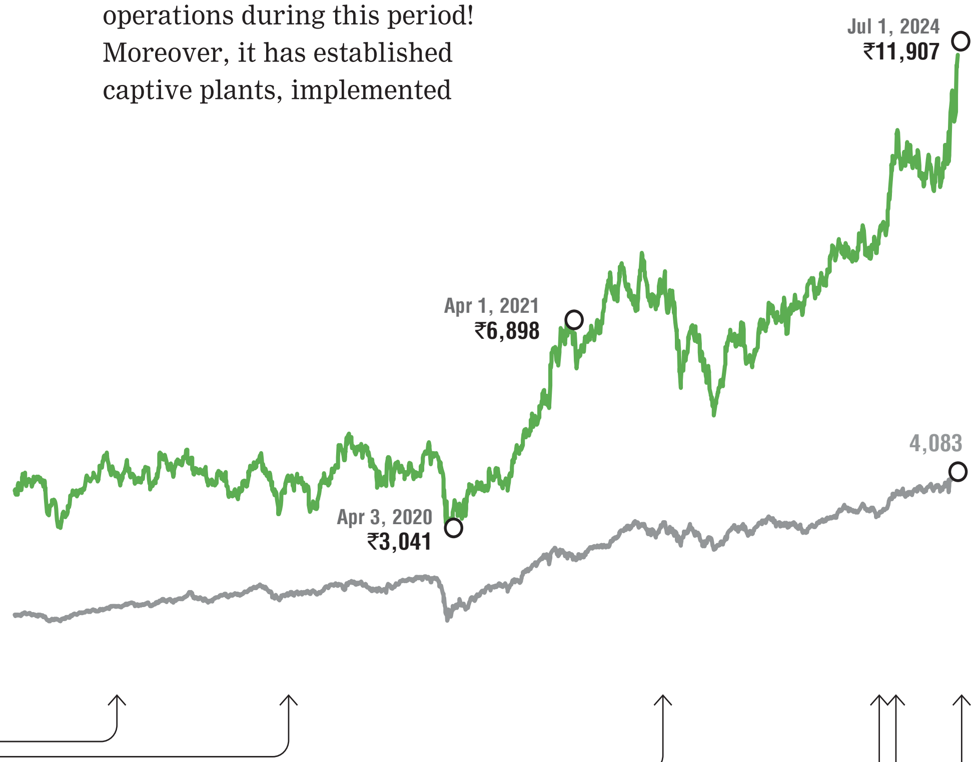
the largest in the cement industry at the time, making the company the eighth-largest cement player in the world. Moreover, with this acquisition, its total capacity leaped to 31 MTPA. The company was listed on the stock exchanges in August 2004.

Decades of excellence

Over the years, the company has primarily focused on building capacities and improving operational efficiencies. Its major acquisitions include ETA Star Cement, the cement business of Jaiprakash Associates, Binani Cements, and most recently, Kesoram Industries. The company has spent ₹48,778 crore on capex in the last 20 years, which is 52 per cent of its cash from operations during this period! Moreover, it has established captive plants, implemented water heat recovery systems and invested in green energy transmissions to reduce costs. Consequently, its revenues and profit after tax grew 19 and 35 per cent annually, with a median ROCE of 14 per cent during FY04-FY24.

UltraTech plans to spend ₹32,400 crore more on capex to increase its capacity to 200 MTPA by FY27 from 150 MTPA as of FY24. The growth in the construction and infrastructure sectors, and the company's robust distribution network will drive its growth. However, UltraTech operates in a cyclical industry and faces competition from other large players that are also scaling up rapidly. ☑

By Vishal Goyal



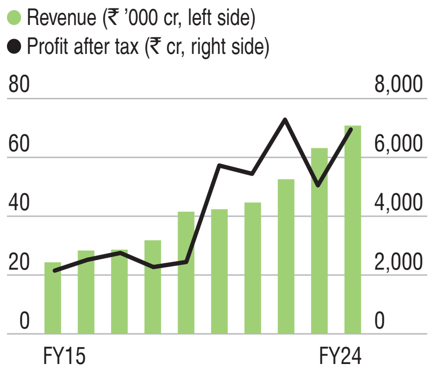
Jan 20, 2022
Acquired complete stake in National Limestone Company.

Oct 27, 2023
Announced an additional ₹13,000 crore capex to add 21.9 MTPA capacity, taking its total capacity to 182 MTPA.

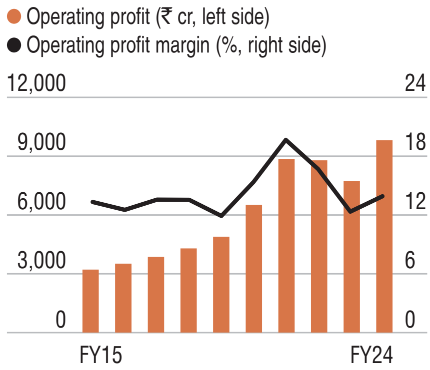
Dec 1, 2023
Acquired the cement business of Kesoram Industries.

Jun 27, 2024
Acquired 23 per cent stake in India Cements for ₹1,885 crore.

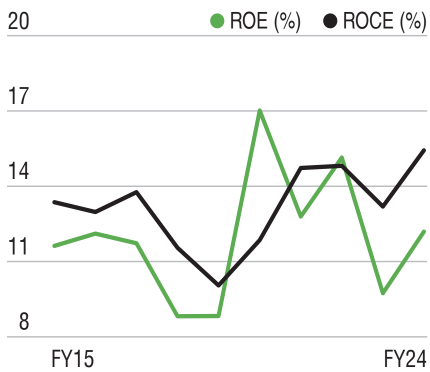
Revenue and profit after tax



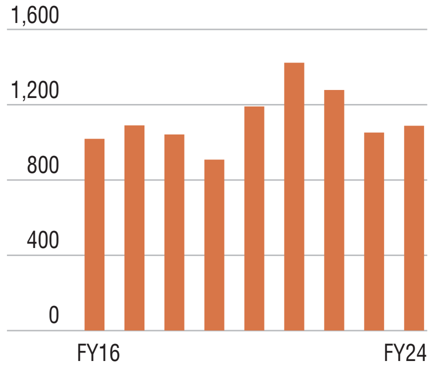
Operating profit and margin



ROE and ROCE



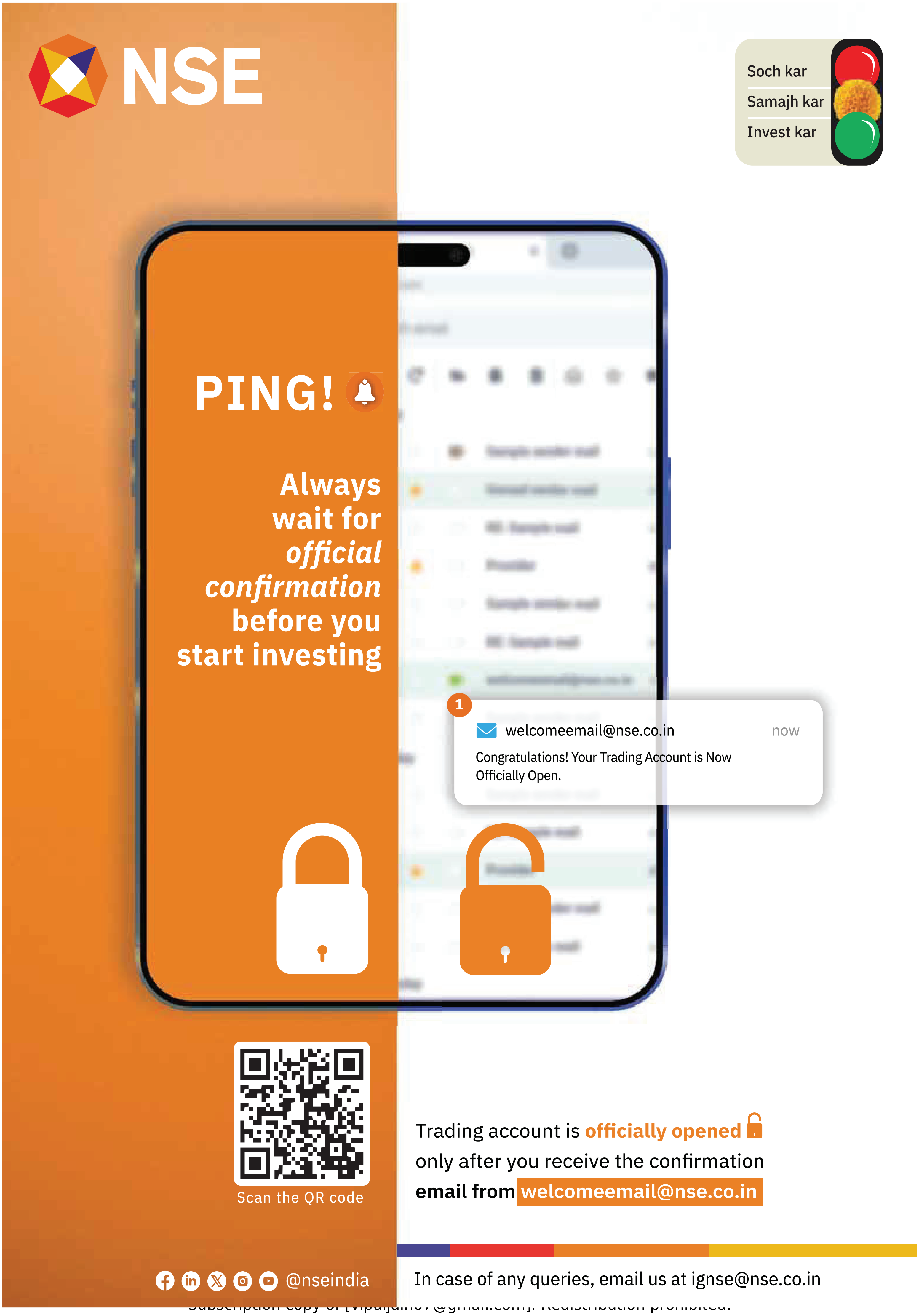
EBITDA per tonne (₹)



Large caps

	Stock Rating	3M returns (%)	Price to earnings	3Y avg RoE (%)	3Y earnings growth (% pa)
Cochin Shipyard Its subsidiary UCSL bagged orders from Adani Group firm Ocean Sparkle	★★★	148.8	92.2	12.5	8.8
Mazagon Dock Won a ₹1,070 crore order for 14 fast patrol vessels	Unrated	143.6	56.1	21.6	45.0
Rail Vikas Nigam Bagged an order worth ₹132 crore from Central Railways	★★	142.8	82.9	20.4	16.8
IREDA Its FY24 profit after tax was up 45 per cent YoY	Unrated	81.1	8.7*	16.0	53.5
Dixon Tech Signed an MoU with Acerpure to manufacture consumer appliances	★★★	67.7	206.3	21.5	31.7
Hindustan Zinc Formed a subsidiary to foray into mineral exploration	★★★★	63.9	35.9	42.9	-0.8
Samvardhana Motherson Its profit after tax grew 89 per cent YoY in Q4 FY24	★★	62.3	50.3	3.2	55.5
Oil India Signed an MoU with FACT for opportunities in the green hydrogen space	★★★★	54.0	16.4	14.0	79.1
IRFC Its Q4 FY24 profit after tax was up 34 per cent YoY	Unrated	52.7	5.8*	14.6	13.3
Hindustan Aeronautics Received a request for proposal (RFP) for 156 light combat helicopters	★★★★	47.9	48.3	26.4	31.5
REC Its FY24 profit after tax grew 27 per cent YoY, its highest-ever	★★★★	47.5	2.4*	21.2	19.1
Prestige Estates Secured a ₹2,001 crore investment deal with ADIA, Kotak AIF	★★	46.0	51.2	22.8	57.6
Supreme Industries Its FY24 profit after tax was up 35 per cent YoY	★★★★	43.0	69.4	23.8	5.0
Solar Industries Received an order from the Indian Army for indigenous drones	★★★★	41.4	129.5	30.5	44.6
CG Power Signed a pact with the Raheja Group to construct a property	★★★★	40.4	77.9	39.2	109.0

*Price-to-book ratio. Our large-cap universe has 140 large companies, making the top 70 per cent of the total market capitalisation. The list mentions the stocks that have fluctuated most wildly in the last three months. Data as of July 15, 2024.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Mid caps

	Stock Rating	3M returns (%)	Price to earnings	3Y avg RoE (%)	3Y earnings growth (% pa)
Garden Reach Shipbuilders Signed a contract with the Bangladesh government to construct ocean tug vessels	★★★	182.3	80.1	15.7	32.5
PTC Industries Partnered with leading defence organisations under the DTIS scheme	★	92.0	485.4	6.1	78.7
Jupiter Wagons Its subsidiary received ARAI nod to make battery-operated LCV	★★★	89.1	89.9	10.7	865.3
GE T&D Bagged an order from Power Grid to build an STAMC in Odisha	★	82.3	236.5	0.3	44.2
Kirloskar Brothers Its FY24 profit after tax was up 51 per cent YoY	★★★	81.0	49.9	12.7	36.3
Jyoti CNC Its Q4 FY24 profit after tax was up 43 per cent YoY	Unrated	80.1	192.9	2.9	32.0
Tejas Networks Its Q4 FY24 profit after tax surged 12 times YoY	★	79.9	386.8	-0.6	18.8
IFCI Received ₹500 crore capital infusion via issuing equity shares to the government	★★★	77.9	3.9*	-100.7	28.6
Bharat Dynamics Its profit after tax surged 89 per cent YoY in Q4 FY24	★★★★	76.2	97.4	12.9	33.5
Titagarh Railsystems BlackRock acquired its shares through block deals	★★	74.4	80.3	7.3	159.0
Techno Electric Bagged orders worth ₹4,063 crore from multiple companies	★★★	73.3	59.8	11.2	14.2
Aegis Logistics Its FY24 profit after tax was up 32 per cent YoY	★★★	65.0	53.5	18.2	36.6
Amara Raja Energy It announced a technology partnership with Gotion Hi-tech	★★★★	65.0	31.3	13.8	10.6
FACT Its share price zoomed on expectations of a healthy monsoon	★★★	62.6	480.6	69.0	-25.3
Hitachi Energy It will invest $1.5 billion to raise global transformer output by 2027	Unrated	59.4	312.1	13.0	14.2

*Price-to-book ratio. Our mid-cap universe has 307 mid-sized companies, making the next 20 per cent of the total market capitalisation. The list mentions the stocks that have fluctuated most wildly in the last three months. Data as of July 15, 2024.


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3 asset classes
1 solution

Small caps

	Stock Rating	3M returns (%)	Price to earnings	3Y avg RoE (%)	3Y earnings growth (% pa)
WPIL Its shares are on an upswing due to general market conditions	★★★★	21.3	9.2	16.8	33.5
Blue Cloud Softech Received CISF recognition for its service at the Hyderabad Airport	★	326.7	325.3	2.4	794.8
Alphalogic Techsys Signed a supplier agreement with Mojj Engineering	Unrated	240.7	414.9	10.6	70.5
Shakti Pumps Secured a patent for a new motor technology	★★	188.6	59.5	15.5	23.3
Tinna Trade Its board approved raising ₹49 crore through equity and warrants	★	161.8	-	-5.7	26.8
Moschip Technologies Secured a contract worth ₹509 crore from C-DAC	★	159.5	548.5	1.0	45.5
Bondada Engineering Received a letter of award worth ₹939 crore from NLC India	Unrated	141.8	133.1	21.8	-
Essar Shipping Essar Group plans to set up a hydrogen plant for ₹30,000 crore	Unrated	140.1	-	-	21.1
Ashima Its FY24 profit after tax jumped over 10 times YoY	★★★	134.6	8.7	3.3	116.9
Tinna Rubber Its shares are gaining due to general market conditions	★★★	116.9	74.4	28.2	223.8
Vashu Bhagnani Its shares are gaining due to general market conditions	★★	104.2	140.9	2.7	429.1
Kaya Marico to handle sales and marketing of Kaya's personal care products	Unrated	92.7	-	-69.2	-211.8
Windsor Machines It was recently acquired by a private equity firm	★★	89.3	-	5.1	-35.8
Dolphin Offshore Its shares are up due to general market conditions	★	83.9	442.1	37.5	40.6
GTL Infrastructure Its loss contracted to ₹681 crore in FY24	Unrated	80.1	-	-	13.5

Our small-cap universe (minimum market capitalisation of ₹750 crore) has 1,096 small-cap companies, making the last 10 per cent of the total market capitalisation. The list mentions the stocks that have fluctuated most wildly in the last three months. Data as of July 15, 2024.

kotak
Mutual Fund

SAPNO KO SKIP NAHI, SIP KARO!

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Mutual fund investments are subject to market risks, read all scheme related documents carefully.

BSE Financial Services

With a three-month return of 8.7 per cent, the BSE Financial Services index was one of the worst performers during the period. In addition, the index has trailed the benchmark consistently in the past few years. Consequently, the index trades at a discount to its five-year median P/E and P/B.

Key numbers

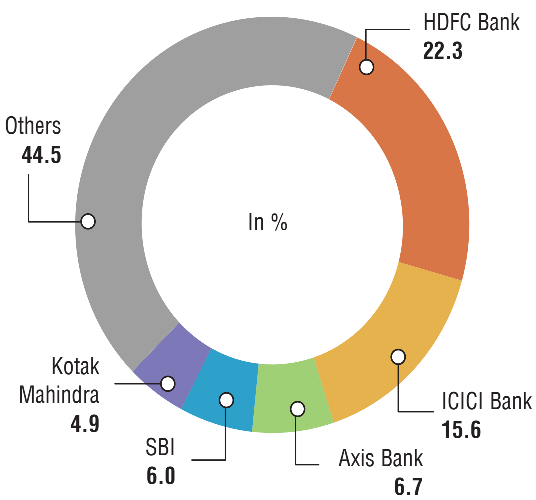
18.1
Price to earnings

2.7
Price to book

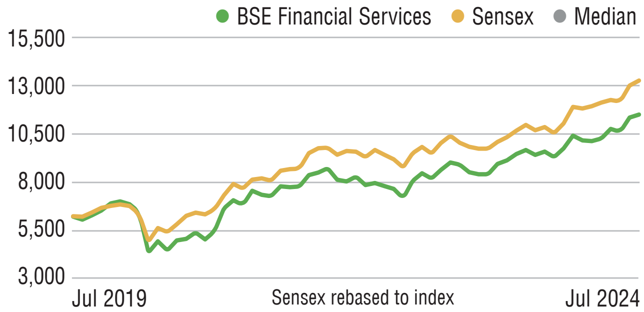
0.85
Dividend yield (%)

99.2
Market cap (₹ lakh cr)

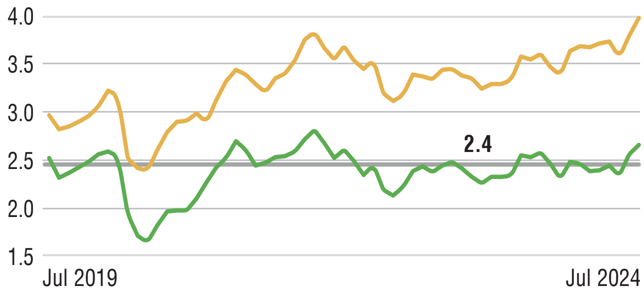
Index weights



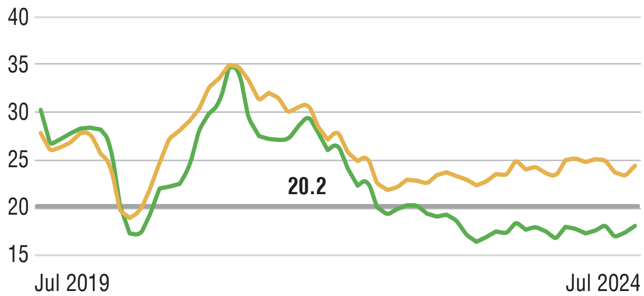
Index movement



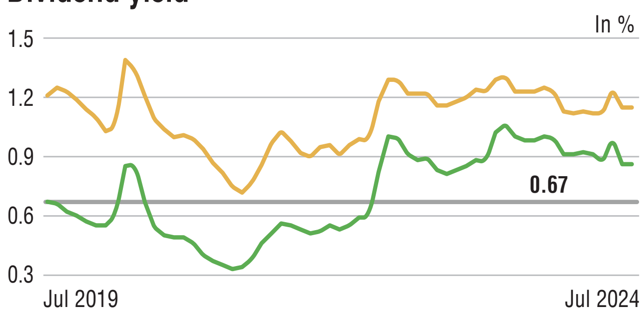
Price-to-book ratio (P/B)



Price-to-earnings ratio (P/E)



Dividend yield



Valuations, dividends and returns

Company	Stock Rating	P/E	P/B	Dividend yield (%)	1Y return (%)
IRFC	Unrated	44.1	5.8	0.7	564.5
IFCI	★★★	190.7	3.9	0.0	504.2
Housing & Urban Dev.	★★★★	31.8	4.1	1.2	468.1
REC	★★★★	11.8	2.4	2.5	295.2
Anand Rathi Wealth	Unrated	66.1	29.2	0.4	275.0
Kalyani Investment	★★★★	40.1	0.3	0.0	241.8
Paisalo Digital	★★	38.1	5.1	0.1	211.4
PFC	★★★	9.3	1.8	2.4	210.4
Dolat Algotech	★★★★★	14.8	2.9	0.2	195.0
PTC India Financial	★★★★	22.3	1.4	1.8	190.5

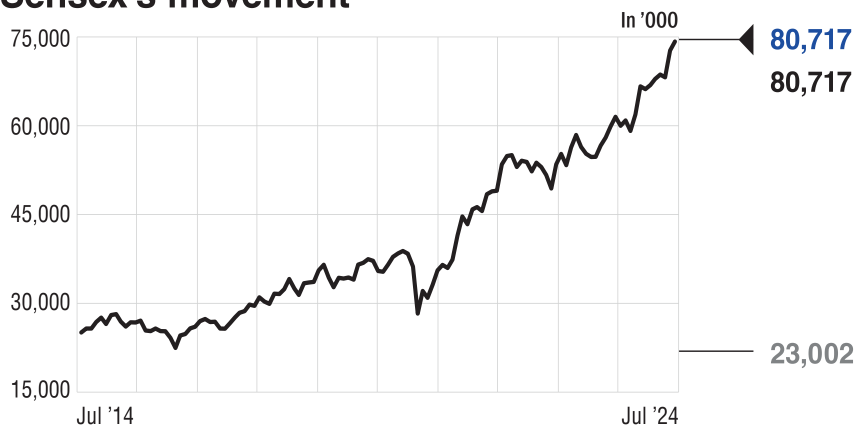
Data as of July 15, 2024

Trends and trails

Here are some charts that will help you make sense of the current market in terms of valuations and return potential

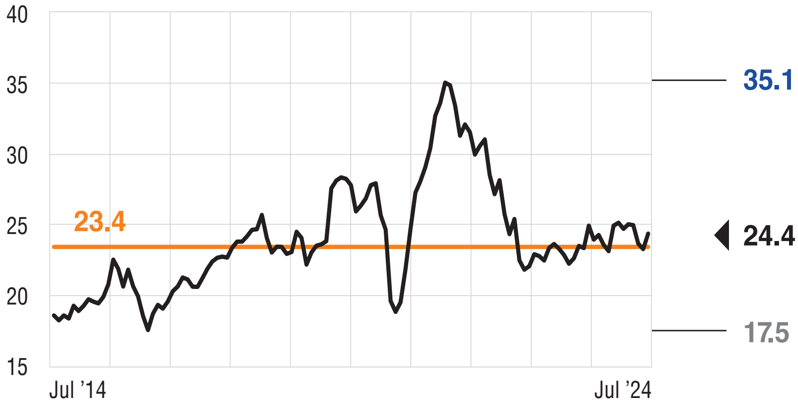
● Max ◀ Current ● Median ● Min

Sensex's movement

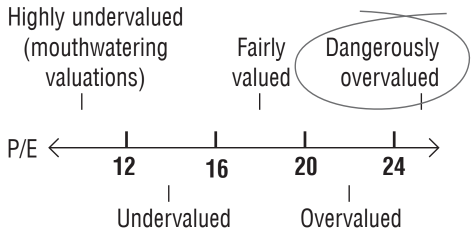


- The Sensex is the most convenient indicator to tell the current state of the Indian market.
- The 10-year graph presented alongside shows the secular run in the markets. However, this rally was punctuated by several bearish phases.
- The most prominent ones include the following: Chinese growth concerns in 2015, demonetisation blues in 2016, the sell-off in 2018 due to US-China trade war and the March 2020 Covid-19 shock.
- After staging a remarkable recovery from the lows of March 2020, the markets yielded to the Russian invasion of Ukraine and rising interest rates.
- With recessionary fears easing and interest rates peaking, the Sensex has been climbing new all-time highs.

Sensex's price-to-earnings ratio

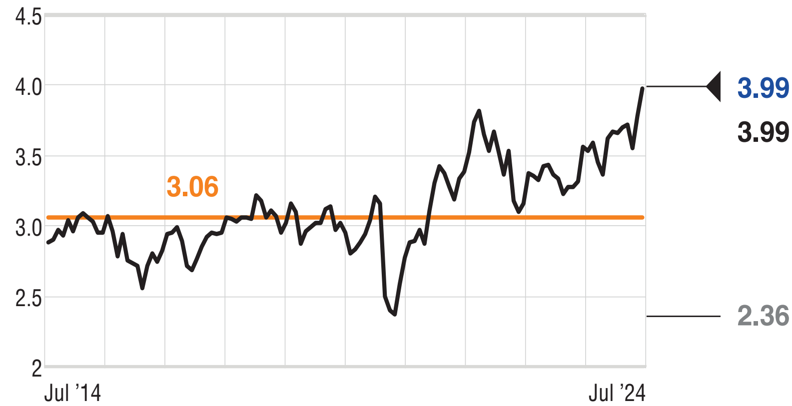


The **price-to-earnings ratio** of the Sensex is a simple market-valuation ratio. A general guideline to help understand the valuation is:



This graph is based on standalone data of Sensex companies. If one takes the consolidated data, the P/E will likely be lower.

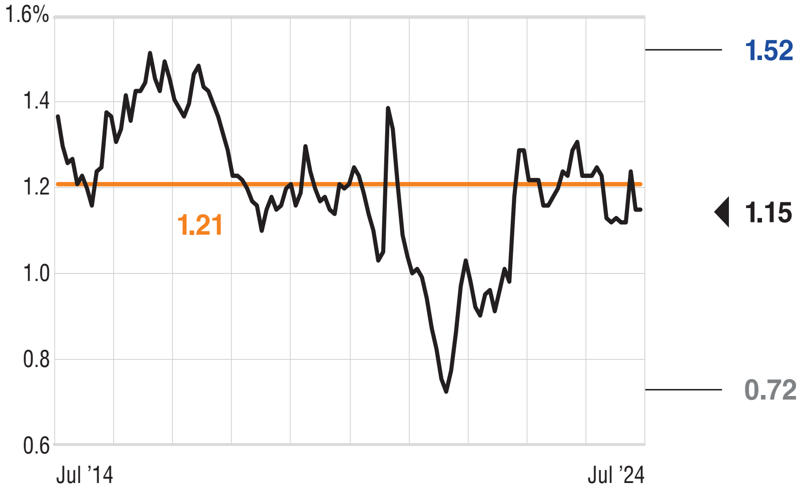
Sensex's price-to-book ratio



The **price-to-book ratio** tells us how many times an investor is ready to pay for a rupee of net assets. Since book value is stable and less volatile than earnings, some consider it better than the P/E as a measure of valuation.

If:
P/B > Median P/B = Overvalued
P/B < Median P/B = Undervalued

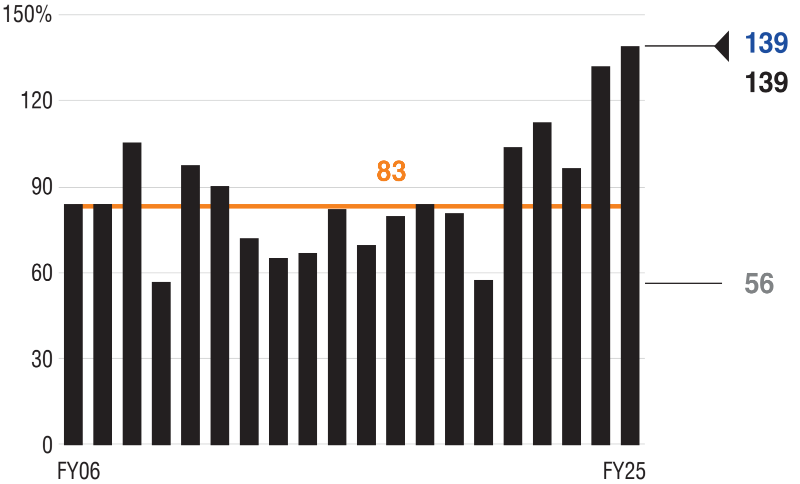
Sensex's dividend yield



Dividend yield is nothing but the return an investor gets in the form of a dividend on their investment. It is measured as dividend per share divided by price per share. Generally speaking, when stocks are cheap, dividend yields are high.

If:
Dividend yield > Median dividend yield = Undervalued
Dividend yield < Median dividend yield = Overvalued

Market cap to GDP



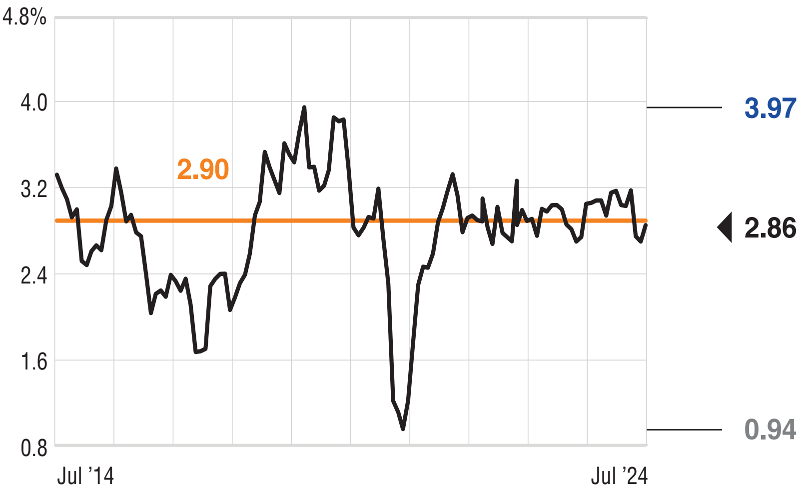
Here, we have considered the **market capitalisation** of all the listed companies on the BSE.

This measure is Buffett's personal favourite. According to him, "It is probably the single best measure of where valuations stand at any given moment."

If:
Market cap > GDP = Overvalued
Market cap < GDP = Undervalued

Considering the market cap of all the listed companies on the BSE, second revised estimate of FY22 nominal GDP, first revised estimate of FY23 nominal GDP and second advance estimate of FY24 nominal GDP.

10Y G-sec yield vs Sensex's earnings yield



The spread between G-sec yield and Sensex's earnings yield is another important valuation measure. G-sec yield is the yield of the 10-year government bond. Sensex's earnings yield is the inverse of its P/E ratio.
The greater the deviation from the median in either direction, the greater the degree of overvaluation or the undervaluation of the Sensex.

If:

Spread > Median = Overvalued
Spread < Median = Undervalued

All data as of July 17, 2024

D-Street debutants

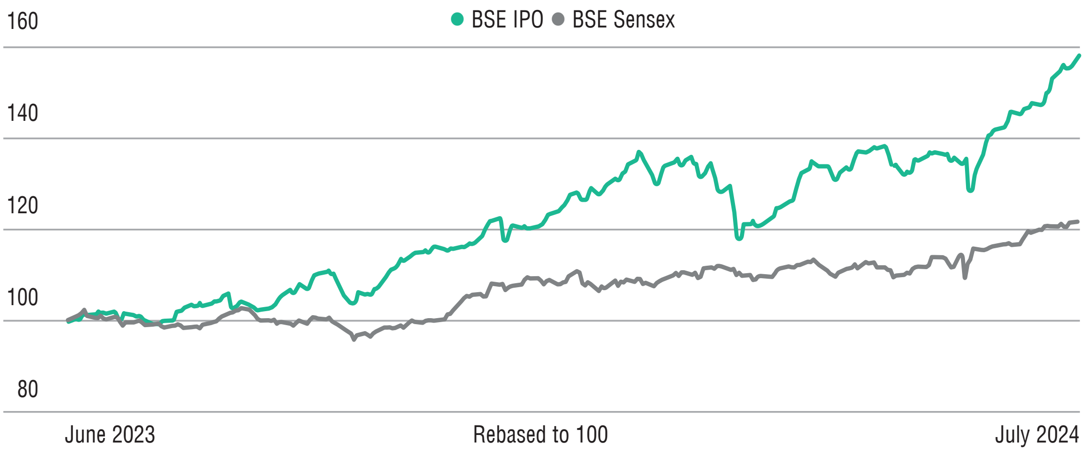
Here is how the S&P BSE IPO Index has performed over the last one year and how the biggest IPOs have fared

Highest listing-day gain
Tata Tech
140.0%

Highest listing-day loss
Gopal Snacks
-12.7%

Highest post-listing gain
IREDA
479.6%

BSE IPO vs BSE Sensex



Highest post-listing loss
Credo Brands
-38.8%

Most subscribed IPO
BLS E-Services
162.5 times

Least subscribed IPO
Popular Vehicles & Serv.
1.2 times

Biggest IPO
Bharti Hexacom
₹4,275 cr

Total issue size
₹63,787 cr

Top 15 IPOs by issue size

Company	Listing date	Subscription ratio (times)	Issue size (₹ cr)	Issue price (₹)	List price (₹)	Current price (₹)	Listing gain (%)	Change post listing (%)	Sensex change (%)	Current P/E
Bharti Hexacom	Apr 12, 2024	29.9	4,275	570	755	1,066	32.5	41.1	8.6	105.6
JSW Infrastructure	Oct 3, 2023	37.4	2,800	119	143	342	20.2	139.3	23.1	62.2
Tata Technologies	Nov 30, 2023	69.4	2,251	500	1,200	1,025	140.0	-14.6	20.4	61.2
RR Kabel	Sep 20, 2023	18.7	1,965	1,035	1,179	1,774	13.9	50.4	20.8	67.1
Indegene	May 13, 2024	69.9	1,843	452	660	576	46.0	-12.6	10.8	41.0
Juniper Hotels	Feb 28, 2024	2.1	1,800	360	361	440	0.3	21.7	11.6	411.1
Honasa Consumer	Nov 7, 2023	7.6	1,702	324	324	480	0.0	48.0	24.2	139.1
Concord Biotech	Aug 18, 2023	24.9	1,551	741	900	1,711	21.5	90.1	24.2	58.1
IREDA	Nov 29, 2023	38.8	1,501	32	50	290	56.3	479.6	20.6	8.7*
Inox India	Dec 21, 2023	61.3	1,459	660	933	1,319	41.4	41.4	13.8	61.1
Go Digit	May 23, 2024	9.6	1,438	272	281	338	3.3	20.2	7.0	170.6
Cello World	Nov 6, 2023	38.9	1,430	648	831	972	28.2	16.9	24.2	64.8
Emcure Pharma	Jul 10, 2024	67.9	1,381	1,008	1,325	1,372	31.5	3.6	0.9	52.1
Samhi Hotels	Sep 22, 2023	5.3	1,370	126	131	183	3.6	40.4	22.2	-
Sai Silks	Sep 27, 2023	4.4	1,201	222	230	174	3.6	-24.6	22.0	26.4

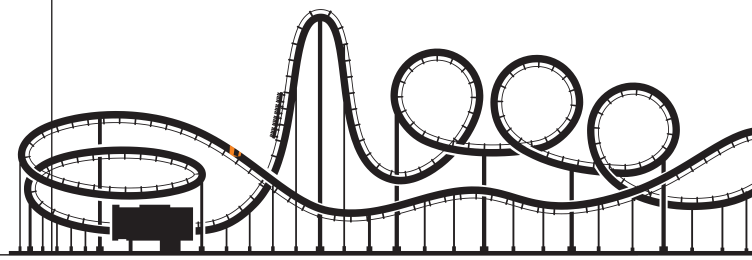
*Price-to-book value. Data as of July 15, 2024.

Mirae Asset Mutual Fund

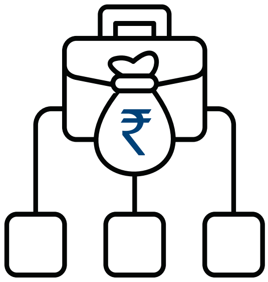
Passive funds for stock investors

Investing in stocks is an empowering experience. You get to **own a piece** of the underlying company's story, becoming a part of its journey.

However, stock-picking is not an easy skill to master. Apart from business acumen, you also need to control your emotions. The market is a **roller coaster of emotions** testing you at every stage. And just like you wear a seat belt on a rollercoaster, you need a metaphoric seat belt for your portfolio too.



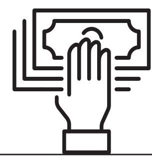
Imagine having exposure to the entire market or different sectors with varied Passive Funds. This **diversification** could help mitigate risks associated with individual stock investments. So, what are passive funds?



These funds, comprising index funds and exchange-traded funds/fund of funds, simply **track an underlying index** and aim to seek to generate returns, subject to tracking error.

For instance, the **Nifty 50 Index** consists of India's top 50 listed companies in terms of market capitalisation. By investing in passive funds tracking such an index, you may seek to get underlying index returns.

Expense ratio matters! Typically passive funds are relatively more cost-efficient than active mutual funds.



Betting against coal

Can Tata Power help you gain from India's march towards a greener future?

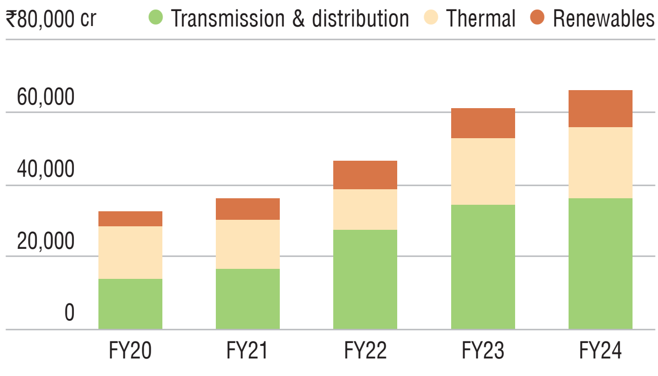
The mercury is climbing, and so is the nation's need for power. In the past two years, India has witnessed two sweltering summers, breaking records held for over a century. A direct consequence of this barrage of heatwaves has been an unprecedented growth in the nation's power demand. The government, too, is buckling up and plans to double the nation's power generation capacity to 870 GW by 2030.

But merely generating more power would be putting a band-aid on a gaping wound. What we need is another green revolution, this time in the energy sector. From the looks of it, we are heading towards that. Of the 870 GW mentioned above, nearly 500 GW may come from renewable sources, says the Indian government.

While these goals are lofty and a lot is still uncertain, investors can count on one thing: Tata Power, India's largest vertically integrated power company, stands to gain from a greener India. But does that make it a perfect investment to ride this green wave? Let's explore.

Turning off the thermal

Revenue share of the thermal segment declined from 45 to 30 per cent between FY20-24



What works in Tata Power's favour

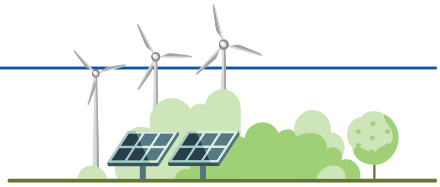
- **Large scale:** Tata Power is a giant when it comes to renewable energy. It generates around 5.9 GW of renewable energy annually, which is around 40 per cent of its total capacity. Also, the management plans to add 5.5 GW to its renewable capacity in the near future. This large stature has already helped Tata Power capitalise on the rising demand for renewables. In FY24, the government auctioned renewable power generation contracts of around 40 GW, nearly four times higher than FY23 levels. Tata Power has won several of these contracts. Also, contracts of around 5 GW are already under execution. Combined, these provide considerable revenue visibility. Going forward, its scale will only expand, leading to further order wins.
- **The solar boost:** The government wants to generate around 40 GW from solar rooftop panels and modules by 2030. Tata Power, India's leading manufacturer of rooftop solar panels with a 20 per cent market share, should benefit from this immensely. In fact, the company boasted a solar panel order book of around ₹16,000 crore as of FY24. The management is also optimistic about adding considerably to its order book in FY25.
- **Better margins ahead:** Renewable energy is cheaper to generate compared to traditional alternatives. Notably, the EBITDA margin of Tata Power's renewable segment was 35 per cent in FY24, double that of the thermal segment. This is especially commendable given that it achieved these margins despite the low capacity utilisation and low margins in the EV charging and rooftop solar businesses. Hence, as the company's energy portfolio becomes renewable-heavy, margins should expand.

But before you rush to click "Buy", remember that no investment is without risks. In the case of Tata Power, we have identified five concerns that should not be ignored.

What works against it

- **The transmission bottleneck.** Tata Power's largest revenue generator is its transmission business, which also happens to be its least profitable venture. The industry has historically battled with high cyclicality and low margins. While recent government initiatives have attempted to minimise these structural bottlenecks, they do not guarantee steady profits for Tata Power.

Minting green



Operating profit has grown significantly since FY20

	FY20	FY21	FY22	FY23	FY24
Revenue (₹ cr)	29,136	32,703	42,816	55,109	61,449
Operating profit (₹ cr)	5,287	4,258	4,348	4,237	6,997
Operating margin (₹ cr)	18.1	13.0	10.2	7.7	11.4
Cash from operation (₹ cr)	7,375	8,345	6,693	7,166	12,596
ROE (%)	6.2	6.1	8.4	12.6	11.3
Debt-to-equity ratio	2.8	2.2	2.1	1.7	1.5

- **Renewables are green, not easy.** You could say renewables are still a sunrise industry in India, suffering from limitations many nascent industries are privy to. Infrastructure for transmitting renewable energy remains inadequate, and a lot is dependent on government policies; the industry is presently riding high on favourable government policies, tailwinds which may not be available perpetually.
- **The China question.** The renewable industry is still reliant on China for raw materials, which exposes the supply chain to macro jolts. None can forget how several industries were left on the lifeline during the Covid pandemic due to their over-reliance on China. Low capacity utilisation. Despite the rising demand, capacity utilisation in the renewables segment was below 30 per cent in FY24. The management has stated that capacity utilisation will improve as thermal power is phased out. However, it is near-impossible to guess a timeline for this to materialise.
- **The ticker is expensive.** The share price of Tata Power has doubled in the past one year. Hence, there's a high chance that the market has already factored in the upcoming surge in earnings, turning valuations expensive. Currently, it trades at a P/E of around 38 times, which is nearly a 46 per cent premium to its five-year median P/E.

Final take

India's march towards a greener future is bound to create several wealth-creation opportunities. Tata Power, undoubtedly, has the potential to be one of them. However, its upcoming growth depends on several factors beyond the management's control. Also, it is important to note that the transition from thermal to renewable energy is a gradual process. Hence, patience is a prerequisite for investing in Tata Power. Apart from that, the energy sector is highly cyclical. Hence, interested investors must ensure that they can stomach the volatility. Also, as is the case for all stock investments, investing at a fair valuation is critical. The present valuation might not sit well with the more value-oriented, conservative investor.

It's crucial to consider all these factors and conduct thorough research before making any investment decisions. Additionally, staying informed about policy changes, market trends, and technological advancements in the renewable sector can provide an edge. ☑

By Hemkesh Khattar

Is this newbie the next underdog winner?

It may benefit immensely from the Delhi-NCR real estate boom

The real estate landscape of Delhi's national capital region is finally getting its long-overdue makeover. The dubious nature of the old, smaller developers of the city has led buyers to look for alternatives. Organised giants like Godrej Properties, Prestige Estates, and DLF are gearing up to fill the part. In fact, the numbers say that the wheels of change are already in motion. In FY24, around 29 of the 83 land deals in the top seven cities happened in the national capital region, says Anarock, a reputed Indian real estate services provider.

But this race to the real estate throne might be turning into a classic underdog story. Max Estate, a small-cap newcomer to the real estate field, is poised to be one of the key beneficiaries of the real estate boom.

Source: maxestatehomes

A bit about Max Estate

Max Estate traces its roots to Max Group, a prominent name in the healthcare industry. The company was hived off from Max India in 2016 and listed in the bourses as Max Ventures and Industries. Initially, the company focused on manufacturing packaging films, with a limited presence in real estate. However, in 2022, it sold its packaging business and relisted in the bourses in November 2023 as Max Estate, a pure-play real estate company.

So, why is the market euphoric about this new kid on the block? It's because it aims to rank among the top real estate developers in Delhi's national capital region. Not just that, it has proved itself to be a formidable contender using its three-pronged growth approach.

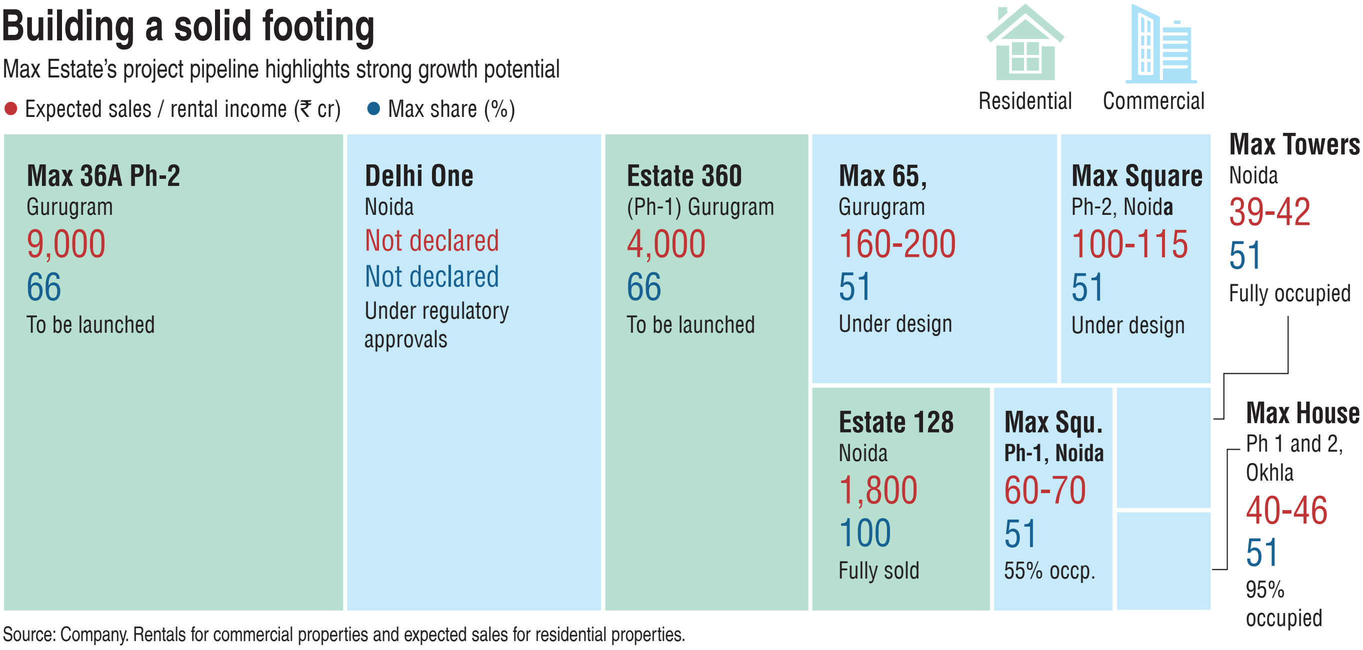
Firing on three throttles

Helio Gracie, one of the founders of Brazilian jiu-jitsu, once said, "A smaller person, if they were to rely on strength, would be exhausted in a short amount of time. So they need to rely on leverage and timing". And it seems like Max Estate is following the same strategy. Instead of going on a land purchasing spree, it is focusing on three key areas where it can have an edge.

- **Reviving ghost projects.** The national capital region is home to several ghost projects, and Max Estate aims to bring some back to life. For instance, it recently completed a distressed project in Noida worth around ₹400 crore. The project offers a 15 per cent rental yield (₹60-70 crore), considerably higher than the average 8 per cent rental yield in the region (as per KnightFrank). Another example would be the Delhi One project started by the 3C Group. The project comprises eight towers encompassing 2.5 to 3 million sq. ft. Max Estate acquired one of the towers in 2017 and has successfully leased out the entire property at 25-30 per cent higher than market rates. It currently awaits Noida Authority approvals for the

Building a solid footing

Max Estate's project pipeline highlights strong growth potential



Source: Company. Rentals for commercial properties and expected sales for residential properties.

other seven towers.

- **Taking the luxury lane.** Max is capitalising on the rising demand for premium housing. It launched its first premium project, Estate 128, in 2023. This project located in Noida has a gross development value (GDV), i.e., the estimated market value of the project upon completion, of ₹1,800 crore. It is also set to launch several premium projects in Gurgaon with a total GDV of around ₹13,000 crore.
- **Keeping the coffers filled.** Funds are often the kryptonite in the real estate industry. However, Max Estate's past in the health insurance industry has helped it partner with New York Life Insurance for its real estate projects. The latter owns a 49 per cent stake in all of Max Estate's commercial projects. Since 2017, New York Life Insurance has invested around ₹1,200 crore in its projects. Apart from this, Max plans to raise around ₹800 crore soon through equity or other convertible financial instruments.

Yet, like all equity investments, Max Estates is not without risks. While the above factors work in its favour, some glaring uncertainties remain.

No rewards without risks

- **Don't disregard delays.** While Max has a lucrative project portfolio, it will translate into revenue and earnings once these projects are delivered. This means that any delay will prolong revenue recognition, impacting financial performance and brand value.
- **Tricky valuations.** Since revenues are recognised post-delivery, valuing real estate players like Max Estate can be tricky; you cannot mindlessly follow price-to-earning multiples. Also, it recorded losses of around ₹55 crore in FY24 due to some exceptional items and marketing expenses, which adds to the valuation conundrum. A workaround would be focusing on cashflows, which stood at around ₹271 crore in FY24.
- **Rising land prices.** Gurugram has recently witnessed an unprecedented rise in land prices. To combat this, Max Estate has resorted to Joint Development Agreements (JDAs) with landowners, wherein the landowners receive one-third of the revenue from the projects. Going forward, landowners may demand higher shares as the land rates continue to climb.

Investors' corner

As always, you must consider if your investment goals and risk appetite align with the above risks and rewards. Also, note that the real estate industry, particularly in Delhi's national capital region, is witnessing an upcycle. However, that might not always be the case, as the real estate sector is highly cyclical. Hence, you must have an appetite for volatility if you plan on investing.

Overall, Max Estate presents a compelling investment opportunity in the current real estate boom, but potential investors should be mindful of the risks that could abruptly end this underdog story. ☑

By Kunal Bansal

ANALYST'S DIARY

Reigniting the forge

One of India's leading forging companies might be scripting a major comeback

Buy the dip. These three words have led countless investors to fortunes. But if you ask us, this market gospel needs a minor modification. You should indeed buy the dip, provided the dip is temporary. And the art of determining whether the decline is a blip or a premonition to losses is what defines an investor's mettle.

This leads us to the curious case of Bharat Forge, one of India's largest forging companies. The company's historical performance does not paint a promising picture.

Yet, in the past one year, the stock has nearly doubled in value. In fact, Bharat Forge's share price went up 42 per cent in the past three months. Unsurprisingly, this made us curious: Is this baseless euphoria, or is something deeper at play? Our research suggests that a comeback is incoming, but with some conditions attached.

More than a spark

The first clue that something grander is underway can be found in Bharat Forge's latest financials. In FY24, the company's profit after tax skyrocketed 77 per cent. Its performance in the final quarter was especially commendable, as profit after tax went up 67 per cent YoY in Q4 FY24. But what is exciting is that these growth rates might not be a one-off. Here's why.

- **Its defence portfolio is finally firing.** Bharat Forge, leveraging its expertise in forging, had started planning its foray into the defence sector as early as 2012. It primarily sought to manufacture armoured vehicles and artillery guns. In 2018, this plan finally came into action, and the company started showcasing its guns at defence expos. The defence sector, at this time, was riding high on several structural tailwinds, namely the Make In India initiative and the revised Defense Procurement Procedure (DPP), which promoted indigenous design and development of defence equipment. Consequently, the defence foray turned into a game-changer for Bharat Forge. From contributing just 1 per cent in FY23, the defence segment accounted for 9 per cent of the revenue in FY24. The company is adding to its capacities to make the most of this defence boom. It plans to double its production capacity in the upcoming years. Furthermore, it is awaiting an lucrative order of Advanced Towed Artillery Gun System (ATAGS).
- **Its international business is recovering.** Bharat Forge is India's leading automotive parts exporter, with over 30 per cent of its revenue coming from overseas (as of FY24). The slowdown in the North American automobile market following the 2008 crash had led to consistent losses in its international operations.

However, the management in the recent earnings calls stated that automobile parts demand is recovering in the North American markets thanks to the EV boom. Aluminium demand, particularly, is surging due to its application in EVs. The management expects this demand to revitalise its overseas operations. The company had also invested around $14 million to acquire Walker Forge, a US-based forging company, in 2016, which should help its prospects in North America. Also, it invested around $60 million (around ₹500 crore) in FY24 on overseas operations and plans to invest an additional $65 million (around ₹540 crore) in the coming years.

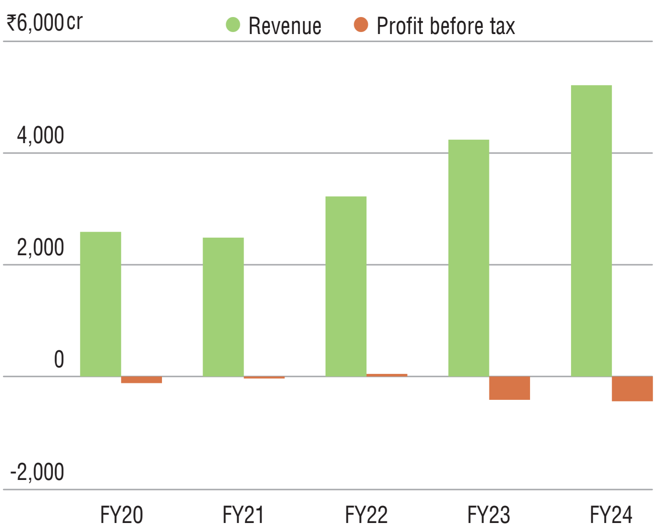
An uninspiring history

Bharat Forge's profit after tax fell 3 per cent annually in the past five years

	FY20	FY21	FY22	FY23	FY24
Revenue (₹ cr)	8,056	6,336	10,461	12,910	15,682
Operating profit (₹ cr)	567	250	1,286	1,032	1,710
Operating profit margin (%)	7.0	3.9	12.3	8.0	10.9
Profit after tax (₹ cr)	392	-97	1,110	542	905
ROCE (%)	6.7	0.8	13.6	8.8	12.1

Overcast in overseas operations

International segment recored losses in four of the last five years



However, not every star has aligned for Bharat Forge. While the above factors hint that a recovery is on its way, several concerns continue to haunt its prospects.

Why the fire may fizzle out

Disregarding valuations can turn even the best of businesses into loss-making propositions. Bharat Forge currently trades at an expensive P/E of 81 times. Some may argue that the upcoming earnings boost will bring down the multiple. However, for that to happen, its share price has to remain stagnant, which seems unlikely.

Apart from the above, two major factors work against Bharat Forge:

- **Low margins in the defence business.** Much of its recovery is expected to be driven by the defence segment. However, the segment has historically been a low-margin venture. For instance, the overall EBITDA margin of Bharat Forge was around 17 per cent in FY24. In contrast, the EBITDA margin of the defence segment was a meagre 4.7 per cent. If margins in this sector fail to improve in the coming years, the recovery will be restricted to the topline.
- **Promoter conflict.** Members of the promoter group, Kalyani, are presently undergoing a legal battle over division of assets. While this is yet to impact business operations, any further escalation may play spoilsport to the company's growth plans.

Investors' corner

Bharat Forge's resurgence has indeed wooed the market. Its future prospects are also promising. However, the present valuations offer no margin of safety, a risk investors should not ignore. Also, note that the defence sector is presently riding high. It is highly possible that domestic demand in this segment will not remain at present levels in the coming years. The demand in the automobile segment is also highly cyclical. Overall, Bharat Forge might stage a grand comeback, but, you need an appetite for risks to be part of the script. ☑

By Satyajit Sen

ANALYST'S DIARY

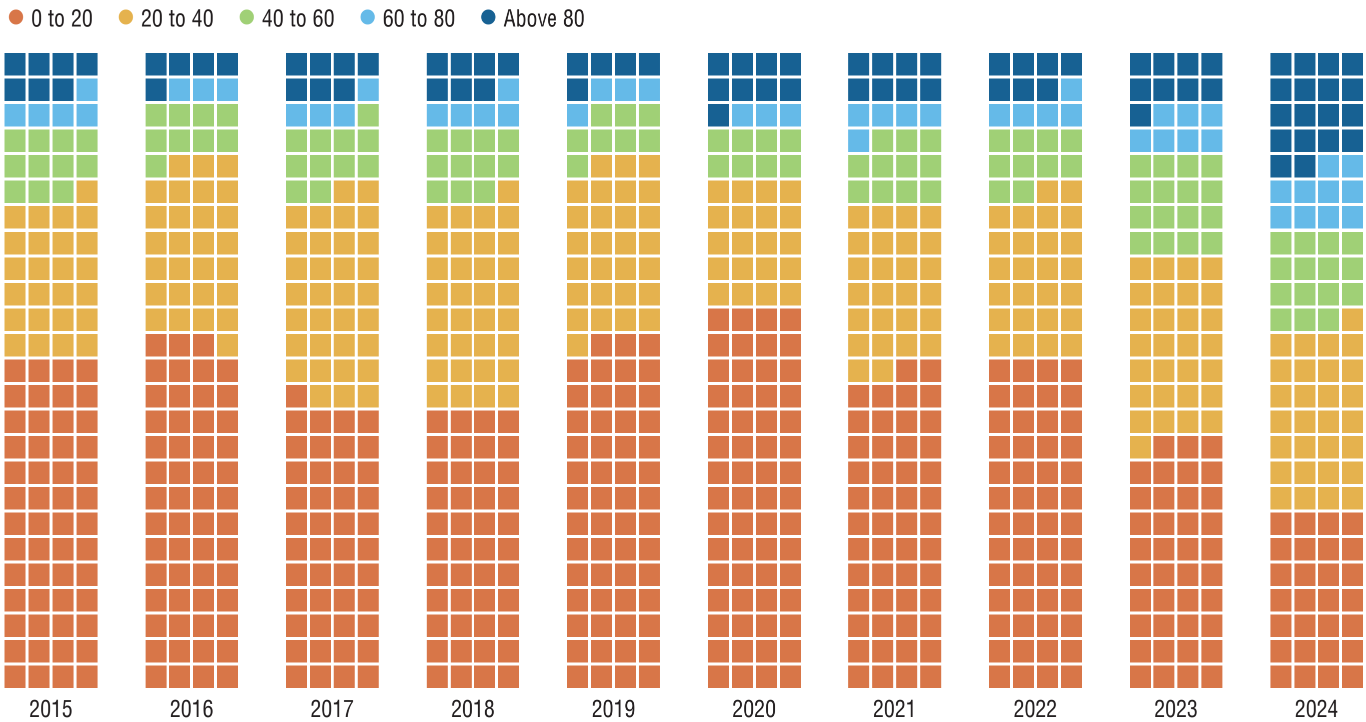
Bursting the bubble

We explore how the recent bull run has inflated valuations

The bull run in the Indian market has led to bloated valuations. The median P/E of all listed non-BFSI companies is presently 36.2 times, which is expensive given that they usually trade at around 19 times their earnings. Also, a record 426 companies (35 per cent of all large, mid and small-cap companies) are trading above a P/E of 50 times. In contrast, only 129 companies or 16 per cent of all large, mid, and small-cap companies traded at these valuations in 2015. Hence, this story

When euphoria runs wild

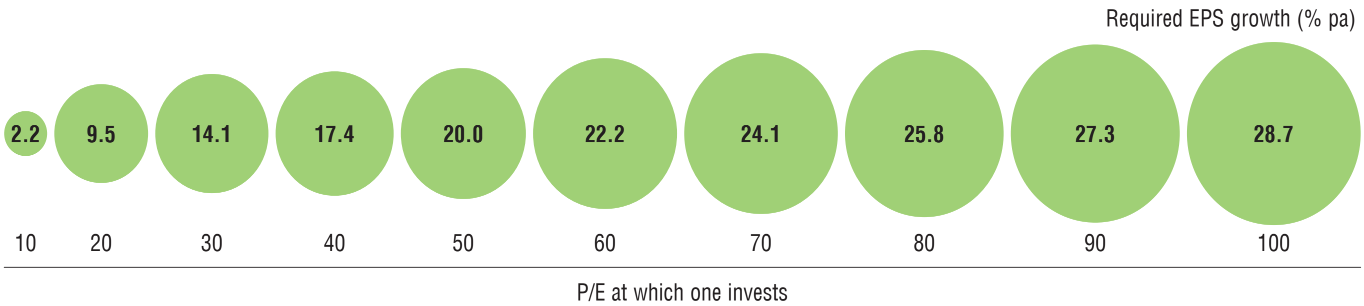
A staggering 216 companies are trading at a P/E of above 80 times



P/E as of last trading day of June of every calender year. Microcaps and BFSI (banking, financial services and insurance) companies have been excluded.

Burden of expectations

As the premiums climb, exponential earnings growth is required to sustain valuations



Investment horizon assumed is 10 years. Required rate of return assumed to be 12 per cent, equal to Sensex's long-term returns. Assuming an exit P/E of 25 times (around long-term average of Sensex).

aims to shed light on the pitfalls of investing at extreme premiums.

Based on the data points presented, it is evident that euphoria is running wild in the market, and valuations are at their peak. As you may know, a high premium means companies must deliver high earnings growth to sustain valuations. So, the question of the hour is whether companies can live up to these expectations.

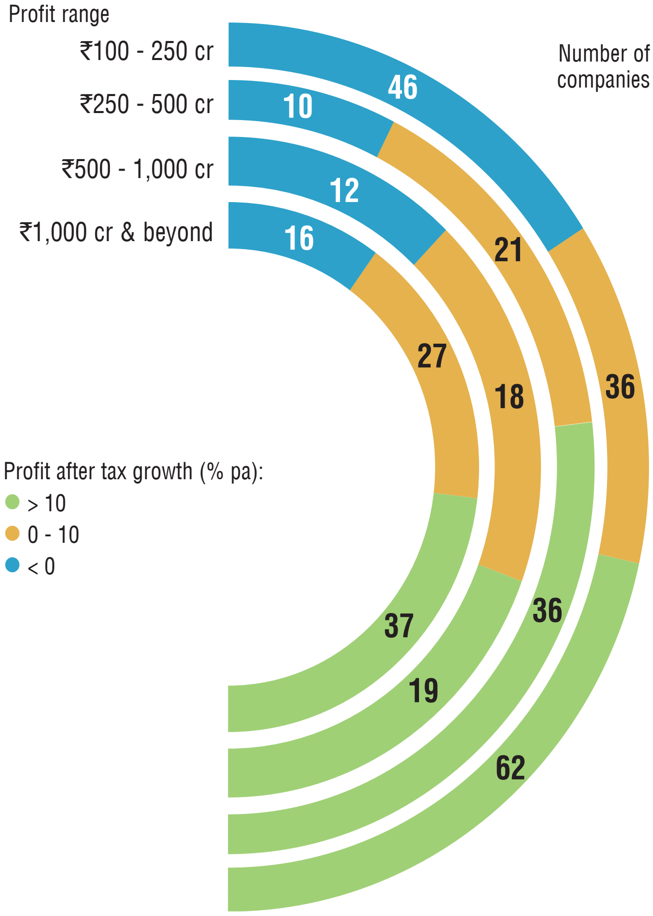
The challenge of sustaining extreme earnings multiples becomes starkly clear from the following thought experiment. Imagine a company trading at 100 times its earnings. To maintain this earnings multiple for 10 years, it must grow its earnings by 28 per cent annually. This means it has to increase its earnings 12 times in 10 years!

Even a small company at the cusp of its growth phase will struggle to achieve this. For bigger companies, it is nearly impossible. For instance, a company earning ₹2,000 crore must grow its profit after tax to ₹24,000 crore!

Unsurprisingly, only three companies have managed to achieve such growth rates in the past decade: Bajaj Finance, JSW Steel, and Torrent Pharma. But, they started from a profit after tax base of ₹100 crore. Over half of all large, mid and small-cap companies failed to compound their earnings by even 10 per cent annually during this period. ☑

A difficult feat

Around 40 per cent of companies in each category have failed to post even 10 per cent annual profit after tax growth



An aftermath of losses

Investing at high valuations mostly leads to capital destruction

Company	Market cap (₹ cr)	5Y return (% pa)	5Y profit after tax growth (% pa)	P/E five years ago
Mishtann Foods	1,861	-2.8	96.5	350.8
Arvind Fashions	6,862	0.3	37.8	240.8
Thomas Cook	11,367	0.9	49.9	101.1
Symphony	8,097	-0.9	10.2	93.4
P&G Hygiene and Health Care	53,951	9.2	12.6	86.3
Shree Cement	1,00,588	5.0	18.7	75.5
3M India	41,482	9.6	11.2	71.5
Dalmia Bharat	34,034	11.6	19.6	65.6
Hindustan Unilever	5,81,571	6.7	11.2	63.9
P&G Health	8,382	4.2	30.3	53.2
Kansai Nerolac	21,830	-1.7	21.3	52.4

Returns as of June 28, 2024. Companies with market cap above ₹1,000 crore have been considered. Excluded BFSI (banking, financial services and insurance) companies.

An investing checklist

In the book, 'Poor Charlie's Almanack,' Peter Kaufman outlines the investing checklist of legendary investor Charlie Munger. Munger, a big proponent of checklists, argues that each of the following principles must be considered part of the larger investment analysis process. That is, these principles should not be viewed in isolation. We have extracted the checklist from the book to help you increase your odds of success. Let's put it to good use!

Illustration: ANAND

Risk

All investment evaluations should begin by measuring risk, especially reputational.

- Incorporate an appropriate margin of safety
- Avoid dealing with people of questionable character
- Insist upon proper compensation for risk assumed
- Always beware of inflation and interest rate exposures
- Avoid big mistakes; shun permanent capital loss

Independence

"Only in fairy tales are emperors told they are naked."

- Objectivity and rationality require independence of thought
- Remember that just because other people agree or disagree with you doesn't make you right or wrong – the only thing that matters is the correctness of your analysis and judgment
- Mimicking the herd invites regression to the mean (merely average performance)

Intellectual humility

Acknowledging what you don't know is the dawning of wisdom.

- Stay within a well-defined circle of competence
- Identify and reconcile disconfirming evidence
- Resist the craving for false precision, false certainties, etc.
- Above all, never fool yourself, and remember that you are the easiest person to fool

Allocation

Proper allocation of capital is an investor's number one job.

- Remember that the highest and best use is always measured by the next best use (opportunity cost)
- Good ideas are rare – when the odds are greatly in your favour, bet (allocate) heavily
- Don't fall in love with an investment – be situation-dependent and opportunity-driven

Decisiveness

When proper circumstances present themselves, act with decisiveness and conviction.

- Be fearful when others are greedy and greedy when others are fearful
- Opportunity doesn't come often, so seize it when it does
- Opportunity meeting the prepared mind – that's the game

Preparation

"The only way to win is to work, work, work, work, and hope to have a few insights."

- Develop into a lifelong self-learner through voracious reading; cultivate curiosity and strive to become a little wiser every day
- More important than the will to win is the will to prepare
- Develop fluency in mental models from the major academic disciplines
- If you want to get smart, the question you have to keep asking is "Why, why, why?"

Analytic rigour

Use of the scientific method and effective checklists minimises errors and omissions.

- Determine value apart from price, progress apart from activity, wealth apart from size
- It is better to remember the obvious than to grasp the esoteric
- Be a business analyst, not a market, macroeconomic, or security analyst
- Consider the totality of risk and effect; look always at potential second-order and higher-level impacts
- Think forward and backward: Invert, always invert

Patience

Resist the natural human bias to act.

- "Compound interest is the eighth wonder of the world" (Einstein); never interrupt it unnecessarily
- Avoid unnecessary transactional taxes and frictional costs; never take action for its own sake
- Be alert for the arrival of luck
- Enjoy the process along with the proceeds, because the process is where you live

Change

Live with change and accept unremovable complexity.

- Recognise and adapt to the true nature of the world around you; don't expect it to adapt to you
- Continually challenge and willingly amend your best-loved ideas
- Recognise reality even when you don't like it – especially when you don't like it

Focus

Keep things simple and remember what you set out to do.

- Remember that reputation and integrity are your most valuable assets – and can be lost in a heartbeat
- Guard against the effects of hubris and boredom
- Don't overlook the obvious by drowning in minutiae
- Be careful to exclude unneeded information or slop: "A small leak can sink a great ship."
- Face your big troubles, don't sweep them under the rug ☑

WORDS WORTH WISDOM

A ‘fan’tastic success

A deep dive into Havells’ unique strategy to capture the fan market

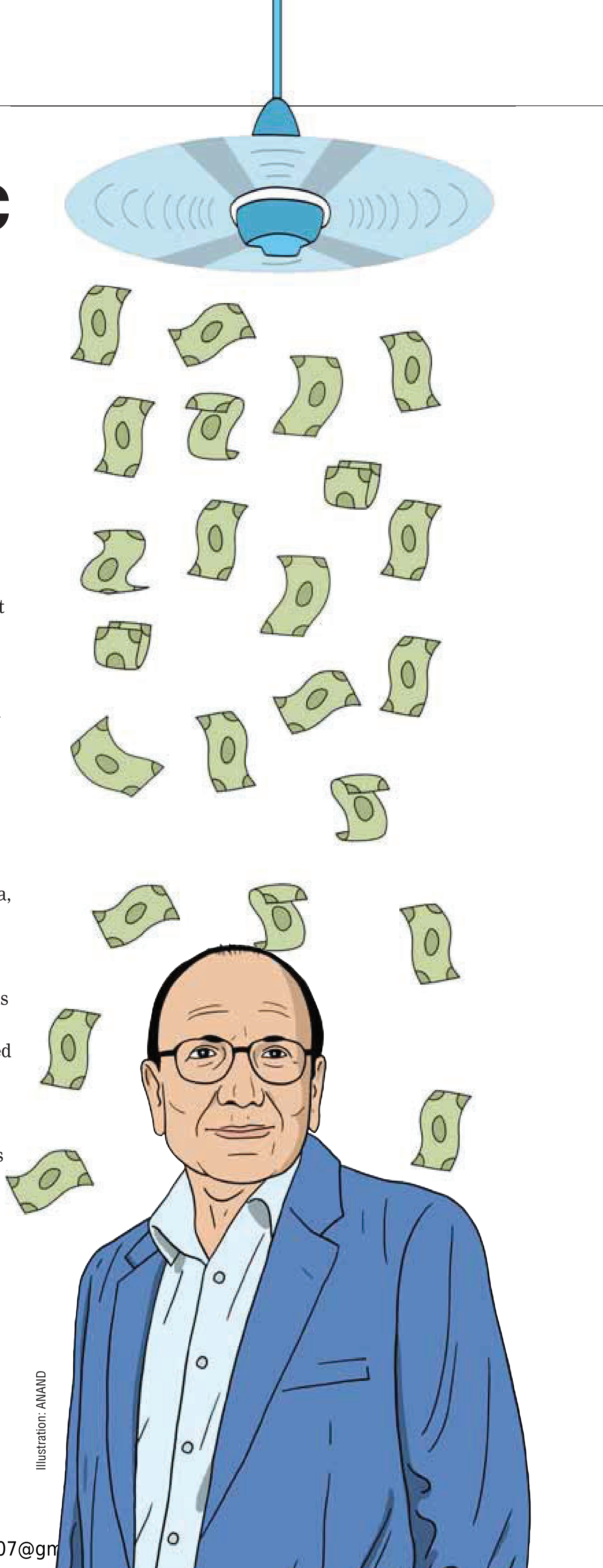


Illustration: ANAND

Havells, a leading player in the electrical goods industry, was once faced with a dilemma. When it exited from the meters segment, its highest revenue contributor in the early 2000s, it had to find new growth avenues. The company could not afford to enter a market where it had to start from scratch. Hence, the only option was to enter a product segment where it could leverage its existing network. That segment was ‘fans’.

In this edition of Wordsworth Wisdom, we’ll look into the book ‘Havells: The Untold Story of Qimat Rai Gupta’ written by his son Anil Rai Gupta, and study what led QRG (Qimat Rai Gupta), the founder of Havells, into the consumer-durable fans segment at a time when many steered clear of the sector.

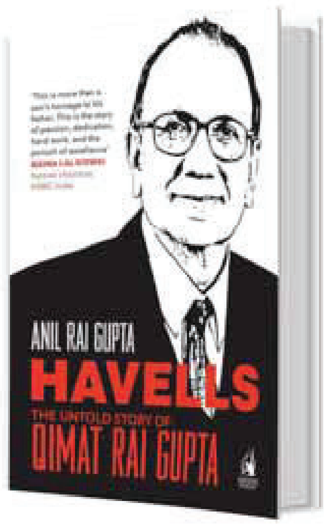
Analysing the market

In 2001, Havells created a small team under B K Gupta, a fan industry veteran, to devise a strategy for entering the market. However, things were far from smooth. “The feedback we got from everybody was that it was not a great space to be in. Six major brands dominated the market – Crompton, Usha, Bajaj, Orient, Polar and Khaitan. No new brand had emerged in the past 25 years, primarily due to the huge presence of unorganised small-scale factories that thrived on evasion of excise duty and used inferior materials to sell at rock-bottom prices. Profit margins were thin, and the market was incredibly price-sensitive,” said Anil Gupta.

Despite these challenges, QRG saw a pattern in another segment, “The wire market had been similar…but we had entered it and done rather well for ourselves”. Similar to the fan industry, the wire segment was largely controlled by unorganised players, who commanded 75 per cent of the market share. Yet Havells had risen to become the second-largest player in the wire market, behind Finolex. QRG believed they could replicate this success in the fan market, but with the condition that “we should

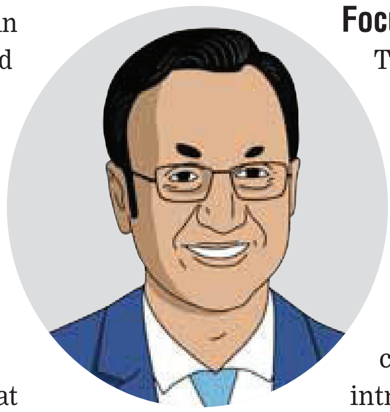
make high-end fans which are backed by a strong brand," and the product would fly off the shelves.

This was when all the naysayers were vocal. "The experts we had appointed also wanted us to make inexpensive fans," Anil Gupta recalls. Existing players were under threat from cheap Chinese imports, and most industry experts believed that competing on price was the only viable strategy.



The turning point

Although the strategy to focus on premium fans seemed absurd to others, QRG believed in it because "the consumers had changed in the 21st century. With an increasing ability to spend, the Indian consumer wanted the best, and she was willing to pay a higher price for it. She also wanted things to be different with USPs. Havells's fans gave her that."



While Sunil Sikka, who joined Havells in 2000, too, had a different plan. He explained QRG's thought process behind this strategy, "My hunch was that having a clutch of products in the same segment at hugely divergent price ranges meant that the cheaper fans would cannibalise the more expensive ones. It also implied that we had to outsource the cheaper products to small-scale units in order to reduce costs and prices, but that meant that we did not have much control over the quality of the products. This is why if one wants to be successful, one has to own plants to control quality."

Hence, Havells introduced a major disruption by rewriting the pricing rules. It steered clear of the economic segment as eventually, "It is easy to work backwards and reduce costs and, hence, prices. But it is impossible to ask the customer to pay a higher price unless the product is of the highest quality. Most industries in India are price-sensitive, especially consumer electrical."

> **"It is easy to work backwards and reduce costs and, hence, prices. But it is impossible to ask the customer to pay a higher price unless the product is of the highest quality."**

This strategy was rooted in QRG's broader philosophy that "companies and brands survive because of the awe and respect they generate in customers largely because of their quality". Havells aimed to build a reputation similar to that of iconic Indian brands, as product quality always reigned supreme in hindsight. Quoting Godrej's example, QRG stated, "Godrej is Godrej. After 100 years of existence, no one says Godrej is a bad company. The products of Hindustan Unilever are always admired. My goal was to be known like them as a quality player. Reputation and image positioning was more important to me than revenues and profits."

Focus on consumers and dealers

To support its premium positioning, Havells invested significantly in branding and advertising. Sikka would reminisce, "We tried to position the fans with varying USPs. For example, for possibly the first time, we talked about how our fans were better in quality; they helped the consumer conserve energy too. We introduced fans with a metallic finish for the first time. We launched, what is now called, decorative fans."

Another tactic that Havells used was to focus on dealers. It offered special incentives to dealers to enable them to concentrate on after-sales services, which was unheard of for consumer durable products like fans. Anil says, "Because of our quality, there were few complaints, but we still thought this would prove useful. It paid off. The trade loved it. Most dealers hate handling angry customers; it is a waste of time and eats into their business. They were happy that Havells took on this responsibility."

This strategy paid off. As per Anil, "The perception and image of Havells soared in the marketplace, both among the consumers and within the trade circles. The dealers were glad to push our brand; in fact, although our advertising expenses went up, most of the publicity was through word of mouth by the dealers." ☑

VIS-A-VIS

Unplugging battery giants

Exploring India's battery leadership

Amara Raja Energy & Mobility

Amara Raja is the largest supplier of batteries to telecom companies and data centres and the largest exporter of 4W batteries. Automotive batteries are its largest revenue generator, accounting for 67 per cent of FY24 revenue, followed by industrial batteries at 24 per cent. The company operates seven manufacturing plants with a capacity of 50 million auto batteries and 2.3 billion Ah (amp hours) industrial batteries.

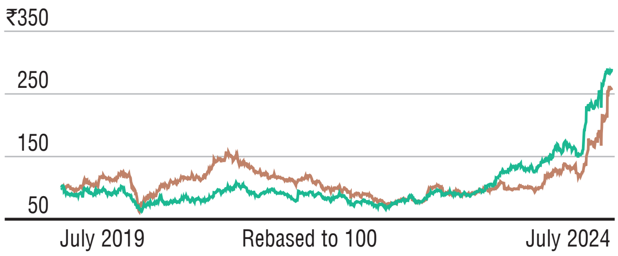
Exide Industries

Exide Industries is India's largest storage battery company. It has 11 manufacturing plants with a capacity of 66 million auto batteries and 6.7 billion Ah industrial batteries. Automotive batteries accounted for 69 per cent of FY24 revenue, followed by industrial batteries at 31 per cent. It also has an international presence, with exports accounting for 10 per cent of FY24 revenue. The two-wheeler industry is its largest client, contributing over half of its FY24 revenue.

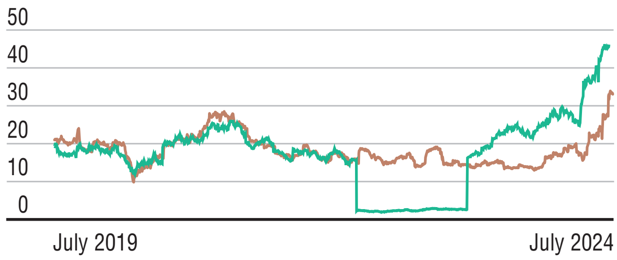
Financials (₹ cr)

Revenue	Operating profit	Net profit	Net worth	Total debt	Cash from operations	Market cap
11,708	1,174	934	6,799	53	1,266	30,373
16,770	1,257	882	12,886	697	1,531	48,671

Price chart



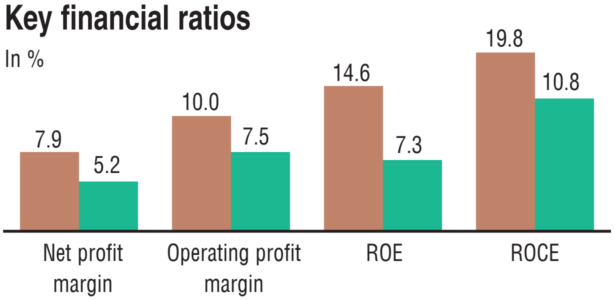
P/E chart



Price to earnings	Price to book	Dividend yield (%)	Debt to equity
33.6 55.1	4.5 3.8	0.6 0.4	0.01 0.05

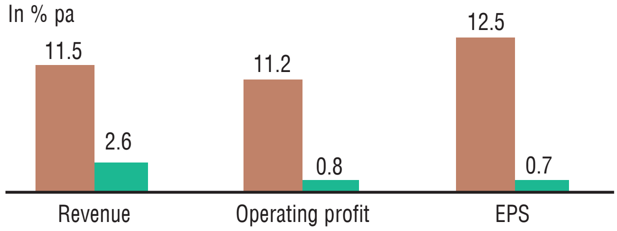
Key financial ratios

In %



Five-year annualised growth

In % pa

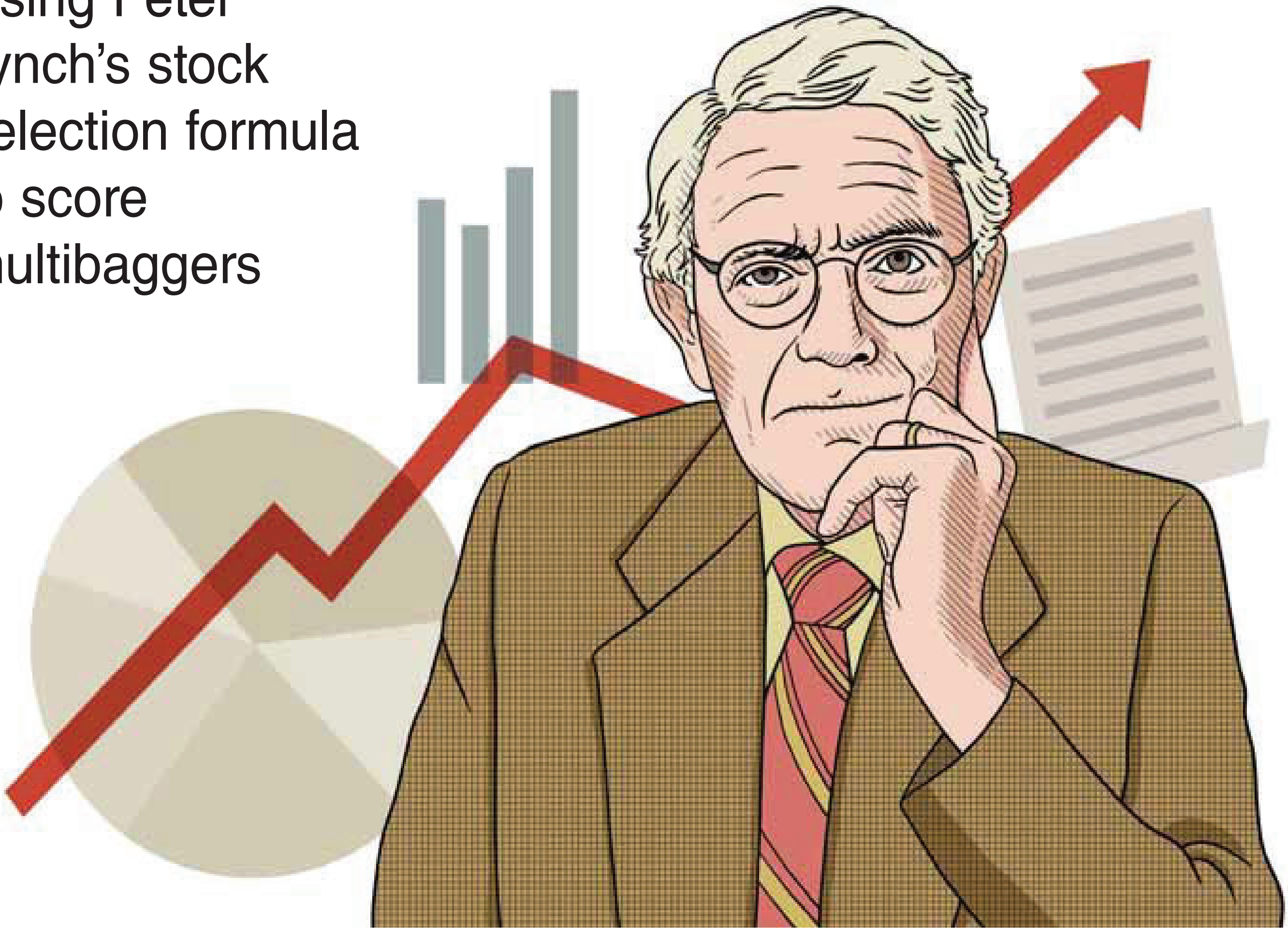


Price data as of July 9, 2024. Financials as of FY24.

The Indian battery industry is riding high on the growing demand for automotive and industrial batteries following a brief period of stagnation. As per a report by Arthur D Little, the automotive battery industry is projected to hit a market size of $1 trillion by 2025. Likewise, the industrial battery market has a promising outlook considering the projected 20 per cent annual growth rate in data centre capacities in the medium term (as per Exide's annual report). Exide and Amara Raja are aggressively investing in the lucrative lithium battery segment, given the government's plan to electrify 30 per cent of all vehicles by 2030. ☑

Profit like Peter Lynch

Using Peter Lynch's stock selection formula to score multibaggers



Illustrations: ANAND

By Udhayaprakash, Kunal Bansal and Harshita Singh

How to succeed as a stock market investor? Aspire to be a chameleon. This is not unsubstantiated advice. We are simply asking you to follow in the footsteps of Wall Street's 'chameleon' and investing genius Peter Lynch, who earned this nickname due to his adaptability to different investment styles to suit prevailing market conditions. This adaptability proved to work as the Magellan Fund at Fidelity Investments, managed by Lynch for 13 years, grew investor wealth 27 times from 1977 to 1990. Not only that, the fund reportedly beat the S&P 500 Index in 11 of the 13 years with an average annual return of 29 per cent.

Lynch's adaptability is a result of his remarkable ability to identify and distinguish businesses based on their varying growth and risk profiles. His book 'One Up on Wall Street', which serves as an investing bible for equity investors, provides us with such an assortment of businesses into six different categories. Each category grasps the unique tenets of a business and relates it to an investing thesis. Since we at Value Research, like many others, are big proponents of Lynch's agile investment style, we attempted to emulate his categorisation framework in this issue of Wealth Insight. Our goal in this story is to understand Lynch's six stock categories and select those that are ideal for long-term wealth creation. We have also built respective methodologies to help you identify promising stocks that fall in the chosen categories. Towards the end of the story, you will discover 10 stocks that fit the Lynch bill. Let's get started!

COVER STORY

The Lynch list

Breaking down Peter Lynch's six stock categories

Before classifying stocks into his six categories, Lynch would want you to place special emphasis on one parameter: the size of the company. In his words, 'big companies don't have big stock moves'.

Simply put, it is difficult for large companies to continue growing at the exponential rates of their yesteryears. Between a company with a market cap of ₹2,000 crore and another with a market cap of ₹2 lakh crore, the former has a high probability and legroom to become a compounder.

Since the company size affects the growth potential, it is a crucial basis for Lynch's first three stock categories where he has primarily used growth as an identifier for solid stocks. Let's go through each of the six categories one by one:

The slow growers

Peter Lynch defines these companies as large, ageing and past their prime. They start as fast growers, but as their size grows and their industry matures, their growth rate plateaus accordingly. Their earnings in this phase may grow just on par with a country's GDP growth. Almost every company and even industries exhaust their initial firepower and eventually reach this stage at some point. Since there is little to no room for growth, there is also no avenue for reinvestment for these companies. While some may attempt using the cash to go the inorganic way, many usually just choose to give generous dividends.

HUL	
6.8	5Y return (% pa)
9.3	5Y EPS growth (% pa)

For instance, FMCG giant Hindustan Unilever's high-teen earnings growth in its early years has slowed to around 10 per cent annually in the last five years. Although it has acquired a few companies over the years like GSK's consumer division, the company is primarily a dividend aristocrat. It has a five-year median dividend payout of 91 per cent!

The stalwarts

These companies are not exactly fast-growing but are still better off than the slow growers. Their earnings growth normally is in lower teens (between 10-20 per cent). Sometimes, they also dole out a part of their earnings as dividends. Since their growth engine has some steam left, investors have the opportunity to reap good capital appreciation, given they invest at the right valuations. Moreover, these businesses are reliable and provide a cushion during difficult times.

Berger Paints	
13.9	5Y return (% pa)
18.8	5Y EPS growth (% pa)

Cummins India and Berger Paints are two examples under this category. The two companies grew their earnings at 18 per cent each annually in the last five years. Their five-year median dividend payout was 56 and 36 per cent, respectively.

The fast growers

Lynch counts this cohort as a goldmine of multibaggers. These are relatively smaller companies that grow aggressively. Their annual earnings growth is usually more than 20 per cent. Generally, these companies are from sunrise industries, but Lynch believes this doesn't always have to be the case. Even in a relatively mature industry, a company can clock high growth rates if it manages to keep grabbing market share from other players. As per Lynch, companies in this category can become 50, 100, or even 200-baggers if held for a long time. But what's crucial to making such returns is catching these companies when they are small. For reference, Dixon Tech's market value five years ago was ₹2,800 crore. The stock has leapt 26 times since then on the back

Dixon Tech	
93.3	5Y return (% pa)
40.6	5Y EPS growth (% pa)

of impressive net profit growth of 42 per cent annually. As a result, it's now holding a market cap of ₹74,000 crore!

The cyclicals

Cyclical companies are those whose revenue and profit expand and contract as the economic cycle changes. During an upcycle, cyclicals perform exceedingly well but during a downcycle, their revenue falls and even profits are wiped off in some cases. Companies in this category are capital intensive and have to rely on both public and private sector capex. Several industries such as automotive, steel, oil and others fall under this category. Tata Steel is an apt example.

Tata Steel

-0.4
5Y returns between 2014-19 (% pa)

27.9
5Y returns between 2019-24 (% pa)

Lynch also highlights how these stocks are often erroneously grouped with stalwarts due to their large size and established brand. Eicher Motors, for instance, is reputed in the auto sector with a market cap of around ₹1.3 lakh crore. It is possible to confuse it as a stalwart given that its five-year annual earnings growth has been around 13 per cent. However, doing so would be incorrect since it is a cyclical business whose profitability is volatile and based on demand for premium bikes. According to Lynch, timing is everything in cyclicals, and to make money in these companies, investors need to be able to detect the cycle's turning points early.

The turnarounds

A turnaround business is the one on the ropes trying to escape a near-collapse or a situation like bankruptcy. Investors can bet on these companies when they expect them to turn the corner. This is because any sign of recovery helps these stocks recoup their lost ground rapidly. Here's a notable example of a successful turnaround – CG Power. The debt-laden and nearly bankrupt company was rescued by Tube Investments, which acquired it for around ₹800 crore. Tube managed to turn around the business, and voila! CG Power's share price jumped 26 times in five years!

CG Power

93.0
5Y return (% pa)

25.9*
5Y EPS growth (% pa)

*– to +

The asset plays

Asset plays are companies with valuable assets that the market has overlooked. Since these assets are not recognised, the real value of the company is expected to be much higher than what the market estimates. These companies may or may not have smooth operations. So, the core investment thesis for them is the assumption that the market will one day catch up to their true worth. The unidentified assets could be plant, land, investments or even cash.

Kama Holdings

9,403
Market cap (₹ cr)

35,679
Market value of its stake in SRF (₹ cr)

Holding companies are good examples of asset plays. The primary reason they grab investor attention is the expectation that their underlying investments' value will appreciate. The higher the gap between their market value and their assumed intrinsic value (including underlying holdings), the more handsome the returns are. Kama Holdings, the holding company of SRF, has yielded an annual return of 37 per cent in the last 10 years, primarily due to the appreciation seen in SRF.

Choosing the right cohort

Zeroing in on the stock categories most feasible for you

We have now understood that companies can broadly fall into one of the six categories defined by Peter Lynch depending on their growth and risk profile. The categorisation makes stock selection easy. But, unlike Lynch, who is a seasoned investor, retail investors do not have the same bandwidth needed to work with stocks across all the groups. This is because most of Lynch's categories are tricky to navigate, and the involved risk-to-reward ratio is unsuitable for small investors. So, we decided to eliminate the cohorts we believe retail investors are better off staying away from. We zeroed down on those that are feasible to navigate and promise tried and true long-term wealth creation. Below are the categories

that we discarded with our rationale for doing so:

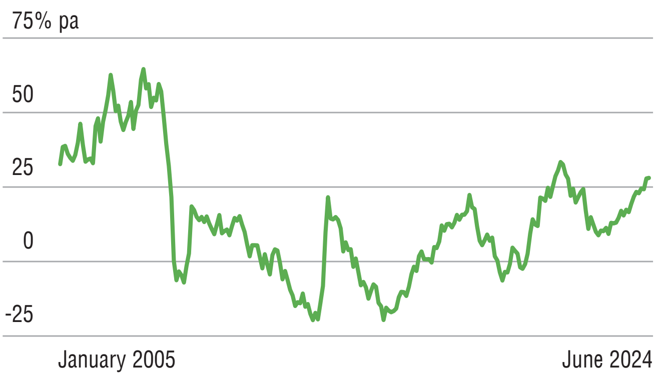
- The first category that we placed off our list is **turnarounds**. These are essentially touch-and-go businesses whose revival is highly uncertain and unguaranteed. For small investors, betting on these companies is, at best, making a prophecy since their assessment is pretty complex. The example of CG Power turning the corners (given in the previous pages) is enticing. But it's important to note that successful turnarounds are not as common as most believe.

  Here's a notable example: SpiceJet was once a promising turnaround story, especially after Ajay Singh acquired a majority stake in the company in 2015. Things did get better for a while before the company again succumbed to high competition and its poor balance sheet. Today, SpiceJet fails to hold its flight in the Indian aviation market. For every CG Power, there are hundreds of SpiceJets that highly skew the risk-return trade-off. It's thus crucial to remember that, more often than not, turnaround companies fail to keep their heads above water.

- The next category that we have ruled out is **cyclicals**. Investing in these companies is the trickiest as it requires getting the entry and exit timing right. Investors need to take bullish positions when the sector/industry is at the tail end of its downturn. It is equally important not to get caught up when the cycle turns the other way by making an exit when it reaches its peak. Even experienced market pundits often find it difficult to assess these entry and exit points. The volatility in these investments is also intense. Refer to chart 'Through boom and bust', where Tata Steel's five-year annual gains of 22 per cent at the end of November 2013 were completely eroded in the following two years as the sector's cycle changed directions. Its five-year returns at the end of September 2015 were -22 per cent.

Through boom and bust

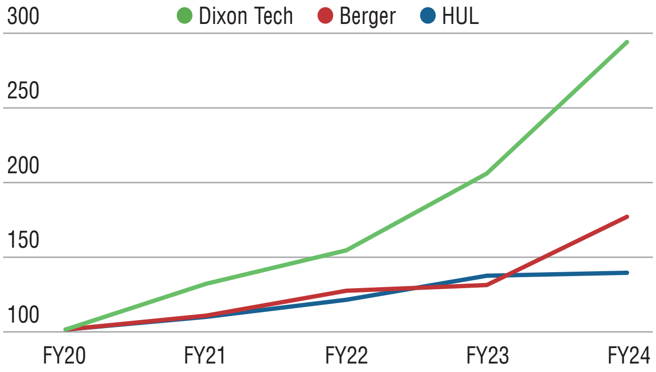
Tata Steel share reflects the company's cyclical nature in its sharp drawdowns and rebounds



Data as of June 30, 2024. Annualised five-year monthly rolling returns.

Resigning to fatigue

Slow grower HUL's EPS lags behind that of stalwart Berger Paints and fast grower Dixon Tech



EPS rebased to 100

- We also dropped out **asset plays** as the only premise for investing in these companies is the realisation of their hidden assets' value. It is impossible to know when and how that will be realised. While investing in holding companies may work since the value of their underlying investments can be assessed, the same may not be possible for companies with assets like plant and land. Unless the company liquidates, investors may never come to know the true value of its assets. Meanwhile, a large cash balance too may not always indicate an accurate unrealised value as many companies burn cash rapidly for fast growth, which often weighs on their overall health.

- **Slow growers** are the most tempting bets of all the categories, given that these are stable large companies with mature operations and a substantial track record of profitability. No doubt, these are the most time-honoured investments in the market, suitable for any investor looking for generous dividend-paying stocks. However, these companies are not much help for those seeking wealth creation as their earnings growth is slow with not much room to expand.

  This leaves us with the **stalwarts** and the **fast growers**. These two categories are cut-and-dried long-term wealth creators compared to the others, given their earnings growth is relatively rapid and they simultaneously offer an optimum risk-to-reward proposition. We delve into these two chosen groups in the next sections.

Safe stalwarts

Our methodology to filter steady and solid stronghold companies

We believe that stalwarts are the safest wealth generators. They are not Peter Lynch's favourites, but nevertheless, he insists on including them in one's portfolio, given they act as defenders during market volatility due to their size and established profitability. To some extent, stalwarts promise the stability and reliability by large, slow growers. But they tend to beat the latter on returns, given their earnings grow faster. Investing in stalwarts at the right valuations is crucial to get impressive returns. We have used unique filters to sift promising stalwart companies in India. We searched for companies that have:

- A market cap of more than ₹15,000 crore to exclude small-cap companies that are usually too volatile to be classified as stalwart.
- A five-year median ROCE of more than 15 per cent
- A five-year annual EPS growth between 10 and 15 per cent.
- A price to equity (P/E) to five-year median P/E of less than 1.5 times.

We used our Value Research Stock Screener to run the above filters and received a list of 29 companies that can be identified as stalwarts. You can find the complete list by scanning the QR code:

Of the 29 players, we handpicked five companies that best suit the category since some cyclicals also happened to appear in the list due to the ongoing upcycle in various industries. It's important to note that a place on this list does not equal a Value Research recommendation. These stocks are worth exploring simply because they fit the criteria of a good investment laid out by Peter Lynch. Please do your own research before investing.

BAYER CROP SCIENCE

Cream of the crop

Bayer Crop primarily caters to small farmers in India who own landholdings of less than two hectares. The company mainly operates in the crop protection segment and sells products like insecticides, fungicides, and herbicides. Some of its recent launches, like Vayego, Council Activ and new hybrids of Dekalb, reported high-single-digit sales in FY24. The company also sells hybrid seeds and provides digital farming services to help farmers improve crop yield and efficiency. Bayer Crop enjoys a unique position in the market as it leverages the capabilities of its strong parentage through Bayer Germany to offer new and innovative products and technologies.

Over the years, it has built a strong distribution network, establishing itself as a trusted brand among small farmers. This has been made possible due to its various partnerships and campaigns. For example, the company's 'Better Life Farming ecosystem' reaches over two crore small farmers, with various institutions like Netafim (for drip irrigation tech) and Axis Bank (for financing), helping it to increase farm incomes. Another of its initiatives is the 'Food Value Chain Partnership', which focuses on collaboration between farmers, processors, traders, and retailers. Some of its renowned partners are Reliance Fresh, PepsiCo, and ITC. All these initiatives place Bayer Crop at the top of the pile in terms of brand recall.

The company is also a cash machine. Its five-year cumulative free cash flows were ₹2,800 crore, and it is nearly debt-free. However, investors must consider that the company operates in a highly competitive market that needs constant product innovation. Further, any negative surprises on the monsoon front risks denting its financials.

12.1
5Y EPS growth (% pa)

39.1
Current P/E

38.8
5Y median P/E

DR LAL PATHLABS

Diagnostic pioneer

Dr Lal PathLabs is India's largest diagnostics chain by revenue and presence. Located pan-India, it provides a wide range of diagnostic offerings, and its brand is well-recognised among end consumers and doctors. The B2C segment made up 73 per cent of its FY24 revenue, while the rest came from institutions and corporates. The company is aggressively focussed on expanding its geographical presence and portfolio offerings. North India constituted 62 per cent of its FY24 revenue with Delhi-NCR alone contributing more than half to this pie.

The company acquired Suburban Diagnostic in 2021 to foray into Western India. Moreover, it is also expanding into tier 3 and 4 cities. It has almost doubled the number of its patient service centres (labs) and pickup points between FY19-24. In terms of product portfolio, it has a wide catalogue of 343 test panels, 3,075 pathology tests and 1,439 radiology and cardiology tests. It is enhancing its high-end test portfolio and has created specialty verticals like Genevolve to focus on genomics and L-CoRD to focus on reproductive diagnostics. Its key offering remains 'Swasthfit', a comprehensive bundled offering, which made up 22 per cent of its FY24 revenue. The company was also among the first in India to offer digital pathology services using high-resolution digitised slides.

The Indian diagnostic market is estimated to grow by double digits over the next five years. In addition, the consumer shift towards organised chains, which currently constitute only 16-20 per cent of the total market, bodes well for the company, given its market leadership. However, the strong growth potential has attracted heavy competition in the sector lately, with hospitals and other chains pursuing growth at the expense of pricing pressures.

12.4
5Y EPS growth (% pa)

65.8
Current P/E

70.5
5Y median P/E

HAVELLS INDIA

Wired for growth

Havells is India's largest fast-moving electronic goods (FMEG) company that sells switches, cables, lighting, and other consumer durables. Cables is the company's largest segment, generating 34 per cent of its revenue, followed by Lloyds at 21 per cent, and other consumer durables at 18 per cent. The company manufactures its products through 15 factories across India.

Havells' core strength is its brand presence. It has become a household name in India's electronics market thanks to its ₹1,748 crore spending on marketing and promotion in the last five years! Another catalyst for its growth in recent years has been portfolio diversification. Its increasing focus on the cables and consumer durables segment paid off, as these two segments posted double-digit annual growth in the last five years. Havells is now among the top five players in all the segments it operates in. Its primary growth driver is to leverage the soaring demand in the consumer durables market and benefit from government initiatives in the cables and lighting segment.

The acquisition of Lloyd from the BR Punj Group has aided its growth as it allowed the company to enter the white goods segment with a strong brand under its belt. Post-acquisition, Lloyd has been the fastest-growing segment for Havells.

But every prize has its price. The fast growth seems to have come at the cost of profitability. Although Llyod was marginally profitable in the first two years post the acquisition, it began clocking back-to-back losses in recent years. In the last three years, it has posted a cumulative loss of ₹465 crore. On top of this, Havells' P/E of 92 times adds to risks.

10.0
5Y EPS growth (% pa)

91.9
Current P/E

68.3
5Y median P/E

KAJARIA CERAMICS

Crafting surfaces

Established in 1988, Kajaria Ceramics is India's largest and the world's eighth-largest tile player. The tile segment contributed 89 per cent to its FY24 revenue, with the remaining share coming from relatively newer segments like bathware (8 per cent), plywood (2 per cent), and adhesives (1 per cent). The company started manufacturing vitrified tiles in 2010, expanding from its traditional ceramics business. The shift towards vitrified tiles was due to their water-resistant nature and the opportunity to earn high margins, creating a better alternative to marble and granite tiles.

Over the years, the company has developed a network of more than 1,800 dealers and 415 exclusive showrooms across India. Its brand spending has been worth over ₹840 crore in the last decade, higher than the overall spending of three major listed peers. The marketing focus has helped the company grab a 10 per cent market share with a pricing premium over its peers. Although the company expects its tiles business to remain dominant in its revenue pie by FY27, the growth in new segments is pegged to be more than double the core tiles segment due to a smaller base and the benefit of the existing dealership network. As most unorganised tile players are export-oriented, this will allow limited domestic competition for branded players like Kajaria. Moreover, the current upcycle in real estate also bodes well for the company. However, one must be vigilant of the potential impact of international markets on the company. Any global slowdown will force unorganised players to increase the domestic supply, or an increase in natural gas prices can hamper the company's margins as they did in FY23.

13.2
5Y EPS growth (% pa)

56.1
Current P/E

47.2
5Y median P/E

L&T TECHNOLOGY SERVICES

The tech trailblazer

LTTS is among India's leading ER&D (engineering, research & development) service providers, with a presence across 25 countries. The company caters to several sectors including automotive, healthcare and industrials, among others. Transportation (automotive) is its largest segment accounting for 33 per cent of revenue as of FY24, followed by telecom at 26 per cent. The company's strength can be attributed to three broad aspects – its client portfolio, R&D and talent. There is fierce competition for highly skilled talent in the industry. LTTS sources talent from various prestigious institutions and through its own programmes. On top of this, it provides consistent in-house training after onboarding employees, further solidifying its talent pool. Its solid talent pool is leveraged for its R&D. As of FY24, the company has 1,296 patents, whose numbers have grown 27 per cent annually in the last five years, highlighting the company's expertise. It went from filing 50 patents every year to every quarter! This has resulted in attracting clients from all over the world. The company has 57 of the world's top 100 ER&D spenders as its clients, with a 90 per cent repeat business. Going forward, it aims to take advantage of the tailwinds in the ER&D industry, which is expected to grow 9 per cent annually until 2030, as guided in its FY24 annual report. LTTS plans to simplify its organisational structure into three broad divisions and has also acquired a company, Smart World and Communication, which has a strong track record in telecom and cybersecurity. But there are a few caveats investors should remember. The company is highly dependent on the North American market, which contributed 55 per cent to its revenue as of FY24. Any slowdown in spending there would drastically affect its growth.

10.8
5Y EPS growth (% pa)

40.9
Current P/E

36.7
5Y median P/E

COVER STORY

Aggressive fast growers

Our framework to sift young high-octane companies

Moving on to our next picks, which are also Peter Lynch's favourites- the fast growers. These are small companies with big growth. While they are not completely risk-free, these stocks have large room to become multibaggers. Lynch believes even one or two of these stocks can be enough to create substantial wealth.We applied the following filters to retrieve promising fast growers:

- A market cap between ₹500-15,000 crore. This eliminates micro caps and companies too large for aggressive compounding.
- A five-year median ROCE of over 12 per cent. This threshold is slightly lower than what was set for stalwarts since fast growers are pretty young.
- Five-year EPS growth of more than 15 per cent annually.
- A five-year annual EPS growth of over 15 per cent.
- A debt-to-equity ratio of less than 2 times and an interest coverage ratio of over 2 times for a healthy balance sheet.
- PEG (price/earnings to growth) ratio of less than 1. Since these companies usually have high P/E ratios on an absolute basis, comparing them with their growth rate is better.

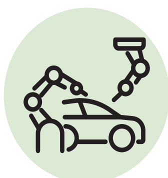
Like previously, we used our Value Research Stock Screener to run these filters, that returned about 163 companies that fall under fast growers. You can find the list by scanning the QR code:

Of the 163 stocks, we have handpicked five companies that have or are building market leadership in a niche sector. We used this as a key criterion as fast-growing companies with a solid presence in distinct markets have higher chances of becoming multibaggers. Please remember not to construe these stocks as recommendations.

CRAFTSMAN AUTOMATION

Automation artisan

Craftsman Automation is a leader in precision manufacturing across many industries. It has three business segments–automotive powertrain, automotive aluminium, and industrial & engineering products making up 35, 48 and 17 per cent of its FY24 revenue, respectively. The company earns about 4 per cent of its revenue from exports. Its automotive powertrain segment caters to CVs, farm equipment, construction and mining equipment, and passenger car segments in the auto industry. Its automotive aluminium products division supplies aluminium components to two and four-wheeler manufacturers. The industrial and engineering segment offers goods and services such as castings, gears, material handling equipment, storage, and other general engineering products to various end-user industries.



24.4
5Y EPS growth (% pa)

45.3
Current P/E

0.85
PEG ratio

The aluminium segment has grown at an impressive 75 per cent annually between FY21-24 on the back of an increasing shift towards electric vehicles. To compensate for the weight of larger batteries, OEMs are opting for aluminium components that have a higher strength-to-weight ratio. The company recently acquired a controlling stake in DR Axion India for ₹375 crore to use its gravity/low-pressure casting processes and increase its presence in the passenger vehicles segment. Further, the company has initiated a greenfield expansion in Kothavadi (Tamil Nadu) and Bhiwadi (Rajasthan). The Bhiwadi facility will bring it closer to many established automakers enabling faster supply and expand its portfolio with them in all its businesses.

However, one should consider the business's cyclical nature due to its dependence on the automobile sector. Raw materials constitute more than half of the company's total expenses, implying that any volatility in input costs can severely impact its margins.

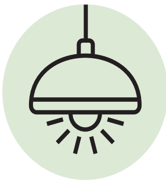
FOCUS LIGHTING

Patenting a bright future

Focus Lighting is probably the youngest and the smallest company by market cap that made through our filters. The company, which started its operations in 2005, provides lighting products and solutions to customers from various segments. Retail is its largest segment contributing 61 per cent to FY24 revenue, followed by the home segment at 31 per cent.

The market is highly competitive, but despite its small scale, Focus is setting itself apart with its unique patents, attracting customers lately. One such patent is for a technology that restricts the spillover of light outside its beam, which allows its customers to use less power for more output. Another patent is for light tunability, which allows customers to modify the light's colour according to the time of the day. It has other patents that revolve around wall washers, glare ratio and more. The company was able to achieve this through its partnership with a German company, Bartenbach. This has led to consistent order inflows from reputed institutions over the years. Focus has also been able to maintain an attractive return on capital, thanks to a combination of higher margins and asset turnover. A P/E ratio of just 25 times makes it more attractive. With more contracts from various organisations, including the government, in the pipeline, the company is confident about keeping up its current momentum. It has won a contract worth around ₹80 crore from the Mumbai Airport.

But there are also risks, one of which is the company size. While it has been on a solid footing lately, the company posted losses during Covid-19, given its small operations could not withstand the industry downturn. It also faces high competition from European players and the Chinese. On top of this, it is also witnessing rising receivables on its books due to high customer concentration.



25.2
5Y EPS growth (% pa)

25.3
Current P/E

0.24
PEG ratio

GRAVITA INDIA

Turning waste to wealth

Gravita India procures non-ferrous scraps and recycles them. The company has established itself as one of the leading recyclers in India and across the globe. It aims to become the most valuable company in the recycling space globally. The company deals in four commodities–lead, aluminium, plastic, and rubber—with lead constituting most (more than three-fourths) of its total volumes. The company has 11 recycling plants and 350 customers across 32 countries.

It benefits from the proximity of its recycling plants near the scrapping and consuming markets, which reduces its freight cost. Further, the high barriers to entry in the market also make it a lucrative bet, given it takes years to establish relationships with OEMs and set up the procurement network the company currently holds. Some of its marquee clients include Glencore, TVS, and Hitachi. Due to the rapid shift towards EVs, the company has forayed into lithium-ion recycling. It has signed a pact to establish a battery recycling plant through a joint venture in Oman, effectively preparing to deal with the slowdown in its lead segment.

The company will also foray into steel and paper recycling. It has marked a capex of over ₹600 crore for the next three years to increase its capacities, with more than one-third of this meant for new verticals. In addition, its shift towards value-added products will further drive margin expansion. The recycling sector is benefitting from various government policies. However, one should take note that Gravita is benefiting more from the formalisation of the market, rather than the overall industry volume growth given it is a slow-growing industry. Moreover, it trades at a P/E of 40, which is more than two times its five-year median P/E.

72.7
5Y EPS growth (% pa)

42.4
Current P/E

0.68
PEG ratio

ION EXCHANGE

The water wizard

Ion Exchange is India's largest water treatment solutions provider. The company's largest vertical is the engineering segment, which provides integrated solutions in water treatment, water waste treatment, and solid waste management. This business made 60 per cent of its FY24 revenue. The second largest, which makes 29 per cent of its revenue, is the chemicals segment, where the company sells various resins and chemicals. Lastly, its consumer segment caters to households, hotels, and other institutions.

The company's early entry into the water treatment segment and its diversified product range have been its biggest advantages. Consistent R&D investments helped the company gain considerable experience over other players, which enabled it to bag contracts from many larger companies and even government agencies. The largest project it has bagged is the integrated water supply solution project for the National Water Supply Board of Sri Lanka. Its consistent R&D also helped it create a diversified product portfolio of chemicals and resins beyond its solutions segment. Although the chemicals segment is the slowest growing, with a five-year annual growth of 11 per cent, it is a high-margin segment with a high return on capital.

The Indian water and environment industry is expected to grow 8.5 per cent annually between 2022-26 with the help of various government initiatives and a growing need for water treatment solutions. Ion Exchange, being the leader, aims to capitalise on this with an order book of ₹3,546 crore in hand. That said, the company is highly dependent on government contracts and initiatives for a major part of its revenue. Any slowdown in orders from the government, or even delay in payments, could dent its financials. Its P/E of 48 times is nearly 2.5 times its five-year median P/E.

24.9
5Y EPS growth (% pa)

48.2
Current P/E

0.19
PEG ratio

MOLD-TEK PACKAGING

Moulded for success

Mold-Tek Packaging is among India's leading players in the plastic packaging industry. With its extensive product portfolio of in-mould labelling, heat transfer labels and decorated containers, the company caters to the diverse packaging needs of the paints, lubes, and the food & FMCG industry. Its client list includes Asian Paints, BPCL and Vadila, among others. Paints is its largest segment, with Asian Paints alone comprising almost one-third of its total sales volume in FY24.

During the past few years, the company has expanded its portfolio, entering into pharmaceutical, sanitiser pumps and QR-coded in-mould label manufacturing, which are high-margin segments. Mold-Tek benefits from its fully backward integrated operations. This means it provides end-to-end solutions in rigid plastic packaging with an in-house tool room capable of making moulds, robots, and IML labels. This reduces its dependence on costly imports, improves margins, and enables quick product development.

The high competition in the paints sector has benefitted Mold-Tek as it grabbed the opportunity to onboard the new entrant in the industry–Grasim. Volumes from the FMCG segment are also growing with the introduction of various new products to develop a wider product portfolio. Although most industries that it caters to have a stable growth trend, several risks remain. For instance, raw material costs constitute more than 50 per cent of its revenue, and one of its key inputs is polymers, a derivative of crude oil. Any fluctuations in global crude oil prices can severely dent its margins. Moreover, its key customer, Asian Paints' other supplier, is an associated entity, Hitech. Any increase in allocation to Hitech by Asian Paints can deal a big blow to Mold-Tek. ☑

18.3
5Y EPS growth (% pa)

40.1
Current P/E

0.60
PEG ratio

All price data as of July 2, 2024

Beginner's ~~luck~~ fears

Value Research Stock Advisor is the perfect antidote to beginner's investment paralysis

by
Dhirendra Kumar

We've all heard of the concept of 'beginner's luck'. However, beginner's luck gets talked about because it's rare. What's actually far more common is beginner's fears. It's scary to start something new, whether college, a job, or equity investing.

It can even happen when you're a legend in your field. Did you know that Sachin Tendulkar would feel nervous at the beginning of each innings? If he needed a moment to settle in, it's natural for new equity investors to seek a gentler start. In fact, his ODI opening partner Sourav Ganguly revealed this while explaining why he often faced the first ball when opening with Sachin. Tendulkar had two reasons: when in form, he wanted to continue his streak from the non-striker's end; when out of form, he needed to ease the pressure. This strategy allowed him to assess the pitch and pace before facing the bowler himself.

Doesn't that sound like a nervous equity investor? When the markets are doing well, you're scared that the bull run is over, or you might pick up some frothy stock. When they're doing badly, well, then they're doing badly, and you're scared anyway.

Is there any antidote to these beginners' fears? Well, that's where Value Research Stock Advisor comes in. Some seven years ago, in October 2017, when we launched this service, we recommended only about 10 stocks. It was easy enough for beginners to understand and quite a comfortable number to start with. Over the years, that list has grown to 50, and obviously, no one is going to start investing with such a large number, and to be honest, neither should they.

Of course, we have a solution to this: our 'Best Buys Now' list. This list highlights roughly 10 stocks from our main list. This doesn't mean the other stocks are less recommended; it simply offers a more manageable starting point for those feeling hesitant, like Tendulkar at the beginning of his innings.

Here are the key points about Best Buys:

The Best Buys list is **not exclusively designed for beginners,** contrary to what some might assume. These carefully selected stocks represent the most promising investment opportunities available at any given time, regardless of an investor's experience level. Whether you're a novice just starting your investment journey or a seasoned investor with years of market experience, these stocks offer compelling propositions. The list is curated based on current market conditions, company performance, and potential for growth, making it a valuable resource for all investors.

By narrowing the focus to approximately a dozen stocks, Best Buys significantly **simplifies the decision-making process** for investors. In a market flooded with options, having a concise list of high-potential stocks can be invaluable. This focused approach helps investors avoid analysis paralysis, which often occurs when faced with too many choices. It allows for a more in-depth examination of each recommended stock, enabling investors to make more informed decisions. The limited selection also makes it easier to monitor and manage investments, particularly for those who may not have the time or resources to track a large number of stocks.

The Best Buys list is **carefully constructed to**

When the markets are doing well, you're scared that...you might pick up some frothy stock. When they're doing badly... you're scared anyway.

Illustration: ANAND

provide a diversified selection of stocks, offering a balanced approach to both risk management and return potential. This portfolio approach is crucial in equity investing, as it helps insulate capital from market volatility while still positioning investors for attractive returns. The list typically includes stocks from various sectors and industries, ensuring that investors aren't overly exposed to any single area of the market.

One of the key strengths of the Best Buys list is its ability to **identify and capitalise on temporary market inefficiencies.** Sometimes, high-quality businesses may see their stock prices decline due to short-term factors or market overreactions. The 'Best Buys Now' feature is designed to spot these situations, highlighting stocks that may be undervalued relative to their long-term potential. By focusing on fundamentally sound companies trading at attractive valuations, this approach aims to exploit market inefficiencies and position investors for potential outperformance as these temporary factors dissipate and the market recognises the true value of these businesses.

In fact, we have a special feature that makes the process of investing in a group of stocks with a given amount of money easier–even if it's a small amount. In our 'Investment Calculator', you can select a group of stocks, enter the amount you'd like to invest, and we'll tell you how many shares to buy. You can play around with the output, adjusting individual stocks and amounts to your liking and arrive at a portfolio.

In equity investing, beginner's fears are natural. The Best Buys list from Value Research Stock Advisor serves as your opening partner, offering a curated selection of promising stocks to help you navigate the market with confidence. Whether you're a novice or a seasoned investor, this focused approach provides a balanced, diversified starting point that capitalises on market opportunities. Remember, as the saying goes, **"The best time to plant a tree was 10 years ago; the second best time is today".** With Best Buys as your guide, you can take that first step towards building your investment portfolio, turning those beginner's fears into a journey of financial growth and learning.

So head over to **www.valueresearchstocks.com,** read more about our features and facilities, become a member, and start investing. ☑

Can infra stocks fulfil their bold promise?

Ashish Naik, Fund Manager at Axis Mutual Fund, is confident that they can

Since 2016, Naik has been a fund manager at Axis AMC, where he currently helms around 18 schemes across various categories. Notably, he co-manages the Axis ELSS Tax Saver and Axis Bluechip funds—the AMC's top two funds with a collective AUM (assets under management) of around ₹71,600 crore.

In this interview, the software engineer turned fund manager shares his outlook on the market.

Recently, the Sensex breached the 80,000 mark. What is your assessment of the market, and what factors are primarily driving its performance?

From an economic point of view, things are and have been decently moving in terms of macroeconomics, fiscal and monetary policies and the fact that there is a certain level of continuity seen from the policy front that the market has appreciated. Risks such as geopolitics and the uncertainty resulting from global political changes will undoubtedly persist.

Over the past few years, India has witnessed the emergence of newer sectors, which likely gained popularity after being absent for nearly a decade. The government's spending, newer policies and PLI (Production Linked Incentive) initiatives have brought these sectors to the forefront. Therefore, we are witnessing a new wave of development in various mid- and small-cap sectors, with some of these developments also evident in large-cap companies. Overall, this has driven the market towards new highs. Even domestic investors, who have consistently entered the market, have played a significant role in this story.

We are witnessing a new wave of development in various mid- and small-cap sectors, with some of these developments also evident in large-caps. Overall, this has driven the market to new highs.

While it's true that Indian valuations are among the highest, a closer examination of growth parameters, as well as ROEs (return on equity) of large-cap companies, reveals a notable positive difference compared to their emerging market counterparts. To that extent, India stands out on both fronts when we compare valuations versus the emerging market peers. Therefore, not all stocks have reasonable prices; many are at significantly higher valuations. If earnings and growth disappoint in these segments, one has to be careful and selective about where they place their bets in this environment.

What factors could derail the rally?

The market rally we have seen is both earnings-driven and valuation-led. Therefore, earnings growth must align with the expectations of various businesses, which poses one of the biggest risks from the stock market perspective. Currently, wherever there are earnings disappointments, stocks have taken a big hit. Such businesses will probably not only underperform for a quarter but maybe for a year or more.

Other than that, we generally don't see many risks on the domestic side. Having said that, when it comes to India, we need to always look at the volatility in oil prices. Due to geopolitical concerns, this risk will always

ASHISH NAIK
Fund Manager, Axis Mutual Fund

remain, and we have to keep that in mind. And that, I think, will be the second biggest risk from the market perspective.

How do you balance between investing in bluechip stocks and high-growth small- or mid-cap stocks?
Regarding fund management, one should strike a fine balance between the fund's mandate and what they are trying to achieve within the fund. Certain fund mandates anticipate a focus on high-growth and cyclical companies, which should be the primary focus of these funds. However, when it comes to a diversified strategy, one would want to have a stable set of bluechip companies that can consistently grow and be more immune to market volatility. This will serve as the fund's foundation.

Given the current environment where cyclicals look particularly strong across various sectors, one can always consider alpha ideas and some form of beta.

What emerging themes or sectors in the stock market are you particularly excited about, and how are you positioning to benefit from them?
One of the biggest themes that we, as an economy, are experiencing is the change from being service-driven to becoming manufacturing-driven. The last decade was mainly about consumption; this decade will be a mix of consumption and investments. Regarding investments, numerous options are available in both the capital expenditure and infrastructure segments. Large-scale manufacturing plants are not comparable to service facilities that primarily require mainly utilities and human resources. A wide range of infrastructure setups are needed for the manufacturing sector, including power utilities, water supplies, port and road connectivity. Plus, establishing a mobile or auto manufacturing unit will also necessitate a variety of ancillaries, leading to a multi-faceted growth story.

Numerous options are available in both the capital expenditure and infrastructure segments... I am confident that this narrative has the potential to endure for a decade or more.

Obviously, these are slightly longer-term, which explains why many stocks in this space appear to be quite expensive in the near-term multiples. So, if they maintain their current growth trajectory and continue to guide and achieve higher targets, they have the potential to provide higher returns. Therefore, I am confident that this narrative has the potential to endure for a decade or more. These are some of the market's most significant changes and themes, driving numerous sub-themes or sub-sectors.

In the past few years, we have seen how higher-end consumption has picked up quite well, and there has been a K-shaped recovery in the economy. At some point, we should also see the lower part of the economy kick in. Furthermore, we can argue that increased spending in the rural sector has the potential to stimulate growth in several other sectors. The third area to consider is the recent surge in real estate, marked by numerous launches. There are sectors that could potentially benefit from the growth in the building materials market. So, many industries look attractive from a medium-term perspective, too.

What indicators or signals do you rely on to judge whether a stock is undervalued?

I believe it's crucial to consider more than just a specific number of valuations when evaluating stocks. Determining a stock's valuation is not just about comparing a particular ratio to its past performance or peers. This is because the market constantly assimilates all available information, and over time, it generally determines the appropriate level for various stocks.

So, what's important here is to understand what can change in the future for that company, for that business or the stock. That, I think, will matter more when it comes to judging if a stock is undervalued. For instance, consider a scenario where the business undergoes a transformation due to internal management changes or external factors such as cyclical or economic shifts. These factors may contribute to a stock's current undervaluation and potentially lead to a higher valuation in the future.

Can you share a key lesson you have learned from a past mistake or challenge in equity investing?

The equity market is fraught with risks. One of the fundamental things I have understood is that assumptions are not absolutes, and one must keep reevaluating them. We base our company valuations on various assumptions such as business, growth and profitability. However, changes are happening rapidly worldwide, which can be due to geopolitical issues and may have a long-lasting impact on a business. Therefore, it's necessary to reassess assumptions, as nothing remains constant. One should keep looking at the thesis and be patient.

The third step is to remain vigilant about who is actually running the business. So, while we are investors, we are also part owners of the company. At the end of the day, someone manages the business, and their ability to achieve success and execute it effectively can be crucial. Poor execution, even with a sound strategy, can be detrimental to a business's success. These are the three key learnings I would like to share, some of which have come from my own mistakes.

Every investor has a story about their first investment. Could you share yours? What company was it, how long did you hold onto it, and what was the outcome?

During my time as an analyst, one of the first sectors I covered involved a particular company that wasn't a household name at the time. I was assigned in-depth research to assess their management's potential for success. This proved particularly challenging, as the company was undergoing a significant shift--transitioning from a domestic to an export-oriented strategy. This bold move ultimately proved to be a game-changer, and the company has become a highly successful investment over the years.

Naturally, the industry had established players. What fascinated me was how this company managed to outperform its well-entrenched competitors. As I mentioned, this underscores the critical role of strong execution and a well-defined strategy. ☑

Bubbles, bubbles everywhere, but not a pin to prick

A surge in investor inflows has led Indian stocks to trade at hefty valuations

By **Anand Tandon**

America's share of the world's stock market capitalisation has climbed consistently over the past decade and a half and sharply this year. It now stands at 61 per cent. That is astonishing dominance for a country that accounts for just over a quarter of global GDP. This has led to warnings that the US market is overheated and may correct. But what of the Indian market?

For the past few years, state-owned companies in India (PSUs or public sector units) have seen a blow-out performance. Companies in sectors like Defence and Railways have seen their stock prices move up by as much as 10 times. This has set the stage for many to factor in years of unrealistic growth. If US stocks are expensive, ours are even more so.

Take the case of Dassault Aviation, the makers of Rafale, and HAL (Hindustan Aeronautics Limited), the makers of Tejas. HAL has benefitted from a slew of orders for Tejas and Prachand, a light combat helicopter. Despite this, HAL's sales have only increased by 10 per cent CAGR in the past three years, even as its margins improved with the government opening up its purse strings. Yet, HAL's order book stands at approximately $11 billion.

As against this, Dassault has witnessed revenues slowing over the past three years. This is now set to change. The forecast growth over the next couple of years is expected to be in the mid-teens, similar to what HAL will see. Dassault is bigger than HAL by almost 44 per cent in terms of sales, with an order book of about $41 billion. What stands out is the valuation – Dassault's EV is a measly $6.8 billion compared to HAL's $41 billion.

And this is not an isolated case. Take the case of shipbuilding. Here are two companies with similar enterprise values of about $12.5 billion. The difference is in their size. Huntington Ingalls's revenues are about 10 times the size of Mazagon Docks. While its growth is a poor 5 per cent compared to last year's 50 per cent for MDL, the question that needs asking is how long we should assume this growth rate for MDL to persist.

A recent report by Kotak Institutional Research analysed what some PSU valuations implied. Take the case of Cochin Shipyard (CSL). Kotak's analysts assumed that CSL was awarded orders for aircraft carriers to the extent that they could not execute anything else. Then, making liberal assumptions on margins and without considering PV (a single carrier takes years to deliver), CSL should have made and delivered 9-13 carriers to the Indian Navy to justify its market cap. The US currently has 11, while China has three.

What are the majority owners doing?

It is easy to argue that the market is sensing and valuing a significant shift in growth potential going forward. Analysts use blunt tools – backwards-looking financials

Indian shipbuilders command a higher valuation

Despite lower growth, investors are willing to pay more for Mazagon than Huntington

	Huntington Ingalls Industries	Mazagon Dock Shipbuilders
Revenue	$12 billion	$1 billion
Operating expenses	$914 million	$183 million
Operating income	$757 million	$159 million
Revenue growth YoY (%)	5	49.3
Gross profit	$2 billion	$342 million
Market value	$10 billion	$13 billion
Enterprise value	$13 billion	$12 billion
P/E ratio	14.2	59.8

Source: Yahoo Finance. Price as of July 12, 2024.

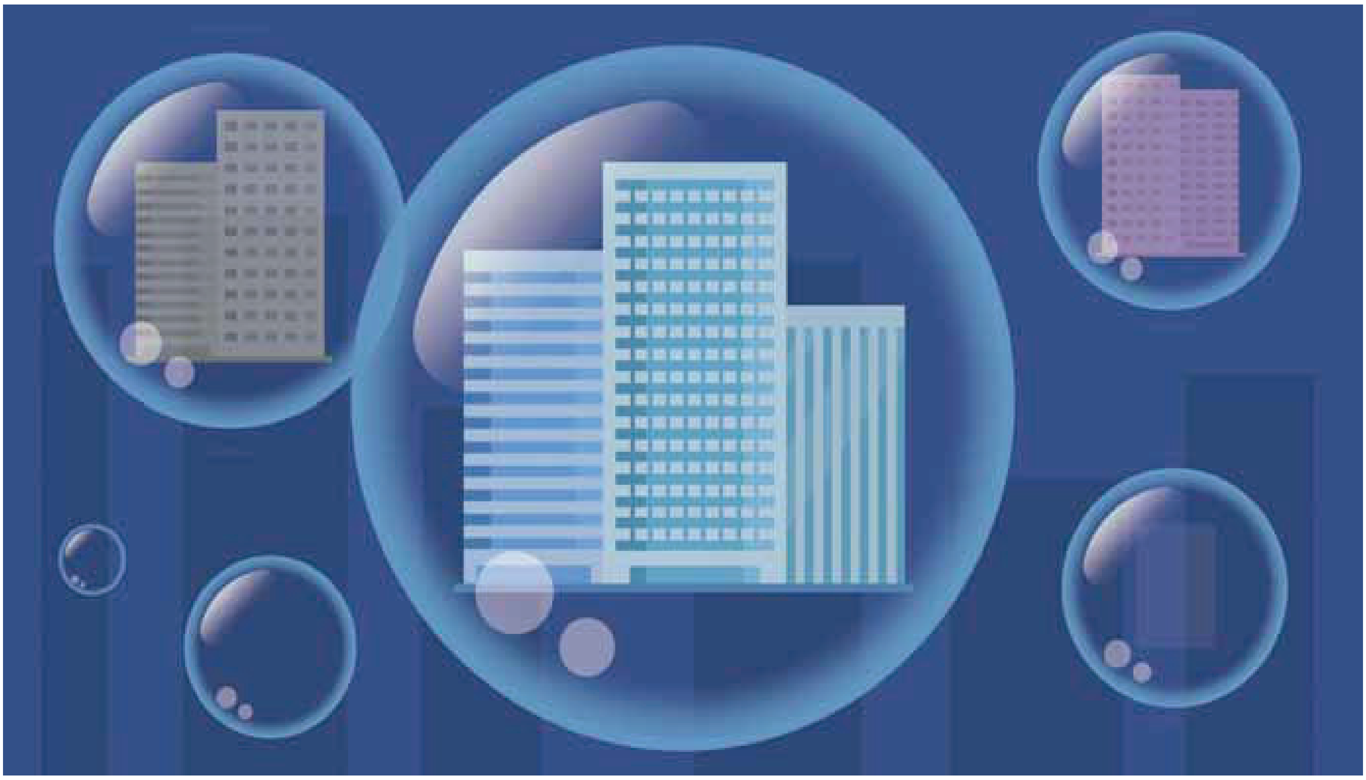


Illustration: ANAND

US defence companies vs India defence companies

Despite lower sales, HAL's market value is more than 3x that of Dassault

	Dassault Aviation	Hindustan Aeronautics
Revenue	$5 billion	$4 billion
Operating expenses	$1.6 billion	$1.4 billion
Operating income	$370 million	$1,000 million
Revenue growth YoY (%)	-	18.2
Gross profit	$2 billion	$2.4 billion
Market value	$14.7 billion	$44 billion
Enterprise value	$7 billion	$41 billion
P/E ratio	20	48.7
Diluted EPS	$9.4	$1.4
Forward dividend & yield	$3.7 (2.0%)	$0.3 (0.5%)

Source: Yahoo Finance. Price as of July 12, 2024.

that fail to capture the reality of a 'new India'.

For a long time, multinational corporations have used every opportunity in the market to increase their stake in their Indian subsidiaries. Unilever PLC is a case in point. Every 5-7 years, the company has attempted to increase its shareholding in HUL (Hindustan Unilever) through open offers. Currently, the reverse is happening.

In recent weeks, BAT sold down its stake in ITC to 25.5 per cent. The 3.5 per cent sale raised ₹17,485 crore. Timken (m-cap $5.87 billion) sold 6.6 per cent of its shares in Timken India Ltd. (m-cap $3.65 billion), ZF Group sold 7.5 per cent of ZF Commercial Vehicles Control System India and Whirlpool raised $468 million to reduce parent debt by selling 24 per cent of its stake in its Indian subsidiary. Speaking to CNBC about the deal in February 2024, Whirlpool's CEO Marc Bitzer said, "In India, we took our shareholding down to 51 per cent. We believe in India for the long term, but if we have a business which is trading at 50 times multiple and your own company (parent entity) trades at a lot lower, it is basic arbitrage". The stock price has since gone up by 55 per cent! The insiders are telling us what they think of their business's prospects compared to what the market is willing to pay.

Are the Indian promoters any different?

Transactions reported through the stock exchanges' bulk/block deal window reveal a rising trend of promoter sales. Though this data will also include sales by foreign companies, it still indicates an increasing trend of selling by promoters in general. Between December 2022 and March 2024, Indian promoters reported a 2.5 per cent reduction in holdings – dropping from 33.1 per cent to 30.6 per cent.

PE investors are finding exits through the secondary market

The markets have provided easy exits to PE (private equity) investors. In the last 15 months (Apr 2023-Jun 2024), PE sales in secondary markets have exceeded ₹1.15 lakh crore. This is reflected in FDI (foreign direct investment) figures, with outflows rising from ₹2.25 lakh crore in FY23 to ₹3.40 lakh crore in FY24.

Offer for sales have witnessed a significant increase. Since April 2023, 91 IPOs (initial public offerings) have raised ₹80,000 crore. Of this amount, 61 per cent has been offer-for-sale while only 14 per cent has been towards 'growth capital'. Over the same period, over ₹1 lakh crore has been raised through QIPs (qualified institutional placements) and FPOs (follow-on public offers).

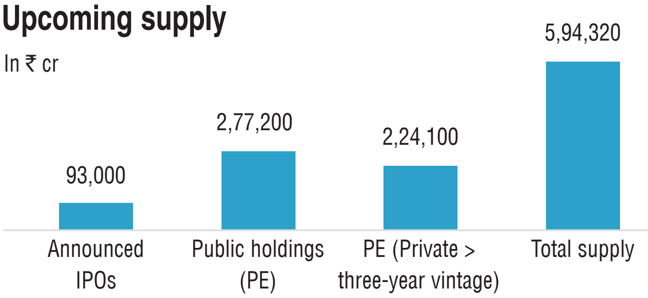
Supply pipeline

In June 2024, mutual funds raised ₹40,608 crore through a combination of NFOs (new fund offerings) and regular inflows – the highest amount raised by the industry so far. Assuming the next 12 months continue to see this inflow, the industry could add another ₹5 lakh crore. On the flip side, the supply side is estimated at almost ₹6 lakh crore. This does not assume any government divestment or increased sales momentum by promoters and multinational companies. The figures are evenly matched.

Domestic investors are extremely confident about the market even as insiders are using the opportunity of high prices to exit the market. Until something changes, momentum is firmly behind the buyers. Government policy needs to be carefully calibrated to ensure that nothing pricks this confidence. ☑

Upcoming supply

In ₹ cr



Source: Axis Mutual Fund Research

The political-corporate tango

How politicians and business people are in cahoots with each other

By
Puja Mehra

The wealthy and their wealth are in the news and on our social media feeds. Beyond the awe and shock, this is a reminder that India's transition to a well-regulated market economy remains incomplete.

No special treatment

Journalists who cover the finance ministry as beat reporters end up running into wealthy business tycoons as part of their everyday work life. In the early 2000s, Anil Ambani was often seen outside Finance Minister Yashwant Sinha's chamber in North Block. Sunil Mittal was a regular visitor to the then Law Minister Arun Jaitley. What was impressive was that suited-booted wealthy visitors were treated no differently than journalists by his Shastri Bhavan office staff. As they waited, everyone was seated in the same room, the office of a member of the minister's staff; there were no special visitor rooms. Government offices weren't as swanky in those days as they are now. It had just been about a decade after the 1991 liberalisation. New regulations in many sectors, such as Telecom, were taking shape. The Atal Bihari Vajpayee government was privatising public sector companies and selling them to private owners. Policymakers and business leaders were, therefore, interacting quite a bit to determine how these big changes were to be navigated. Ministers saw no reason to meet with business people anywhere other than their offices.

Business people used to be friendlier. As a young trainee reporter, barely weeks into my first job, I was delayed (by a sudden spell of rain, if I recall correctly) for a very important press conference by Ratan Tata on the tie-up with Singapore Airlines for buying the government's Air India shares that Minister of Disinvestment Arun Shourie was trying to sell. As there was no YouTube or multiple TV channels in those days to fall back on, I made up by getting the details of the briefing that I'd missed from a senior member of his staff. But I wasn't prepared for what came next – he pulled Tata aside and said to him that since I was fresh out of college, it'd be nice for him to take my questions separately so that I'd have exclusive quotes! Tata, with his old-world decency and courteousness, chatted me up, explained the story of the day, and, as I hurriedly jotted it all in my notebook, started talking about my college. When I said that the library is called '*Ratan Tata Library*', he replied, "You do know that the '*Ratan Tata*' it's named after isn't me." I nodded. He thanked me for the conversation, ended it politely and rejoined the top brass of the Tatas in the room.

During the tenure of the Manmohan Singh government, I recall seeing Lakshmi and Aditya Mittal, talkative and bubbling with excitement, smiles running ear to ear, as they waited to see Finance Minister P Chidambaram. They had just acquired Arcelor. We were in the office of the minister's personal secretary, a bright IAS officer. In this phase, the India-based businesses, too, big and small, were expanding their global presence. The Tatas bought a handful of companies, from the iconic Jaguar Land Rover to Corus. Government offices used to be modest. Meetings between businesses and governments were conducted in *sarkari* offices.

Things take a turn

The noisy narrative of a so-called '2G spectrum scam' in the late 2010s changed all this. No evidence for any hanky-panky could be produced in courts. The

Government offices in the early 2000s weren't as swanky as now. Ministers saw no reason to meet with business people anywhere other than their offices.

Illustration: ANAND

accused were acquitted. Government dealings with businesses changed. Ministers stopped meeting with business tycoons in offices. I haven't spotted a business leader even once in the North Block or any other government office. Presumably, all dialogue on policy matters is conducted in private. It is unlikely that all business-politician dealings earlier were done in the offices. A lot must certainly have been conducted outside of the public glare. But now all dealings are likely to have shifted to the stealth mode, possibly due to the electoral bonds scheme that was declared 'unconstitutional' by the Supreme Court this year.

Crony capitalism prevails

These anecdotal observations tally with India's high ranking in the crony capitalism index that *The Economist* magazine brings out – the 2023 iteration found that over the past decade, wealth from crony-capitalist sectors in India rose from 5 to 8 per cent of GDP. India was ranked 10th out of the 43 countries in the pecking order for exhibiting crony capitalism.

The index was first devised in 2014 when India had ranked ninth among 22 countries and captures the concentration of wealth among a few big business tycoons chiefly due to their closeness to the state. Its measure of crony capitalism is the billionaires' earnings from the 'rent-seeking' sectors, which means the sectors where the business surpluses come from competition-distorting behaviour. This behaviour thrives where the state is involved, and markets can't function as per fixed rules and regulations. Businesses manage to get land, labour and other resources at a concession to prevailing market prices and are able to sell their output at prices higher than what would be in well-functioning markets, such as by forming cartels or being monopolies, all of which are examples of rent-seeking behaviour.

The Economist considered the following as rent-seeking sectors – casinos, coal, palm oil and timber, defence, deposit-taking banks and investment banking, infrastructure and pipelines, oil, gas, chemicals and other energy, ports, airports, real estate and construction, steel, other metals, mining and construction, utilities and telecom services.

In the 2023 iteration of the index, Russia, predictably, was placed in the first position. China was at number 21 despite having numerous billionaires; its ranking fell over the years as tycoons took their businesses to other countries. The US, a lot less a crony-capitalist country, was ranked 26th but could quickly rise up the pecking order if the Big Tech is designated as a crony capitalist sector, given tech firms are big lobbyists in Washington. Doing so, the magazine wrote, would increase America's crony wealth from 2 to 6 per cent of GDP. Germany, of course, came out as one of the least crony-capitalist countries at 37.

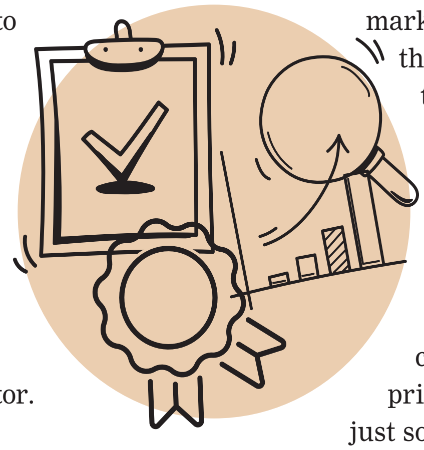
The index isn't as elegantly constructed as the famed Big Mac index, which helps compare prices across countries. It is criticised for oversimplifying the measurement of something as complex as the business-political nexus. Still, it shows how much wealth is being made by simply bending the rules and getting friendly with politicians. ☑

Puja Mehra is a Delhi-based journalist and the author of 'The Lost Decade (2008-18): How the India Growth Story Devolved into Growth Without a Story'

Blue chips and quality stocks at bargain

These stock screens filter attractive large caps and fairly priced quality stocks

A stock screen filters out companies based on certain criteria. Its main advantage is that it helps you generate stock ideas with just a few clicks. Once you have the list of 'deserving' stocks, you can research them further to find the ones worth investing in. The Value Research website provides you many ready-made stock screens. This month, we will be covering two such screens: 'attractive blue chips' and 'discount-to-book value'. We have also given a concise stock list from the other screens. To get the full list in real time, visit www.valueresearchonline.com/stocks/selector.



What do these screens offer?

The first screen gives blue-chip companies at attractive valuations, while the second screen offers companies that pass the basic quality parameters and are available at cheap valuations.

Attractive blue chips: Blue-chip stocks are the largest and the most consistently profitable companies. Owing to their strong balance sheet and high market share, they are less risky than their smaller counterparts. However, these stocks have already been 'discovered' (i.e., known to most investors). For this reason, they generally trade at a premium.

Quality stocks for cheap: A core principle that we follow when looking for stocks is that quality cannot be compromised for reasonable prices. What we mean by quality is not just solid financial metrics but also business fundamentals related to management transparency, accounting practices, among others. So, we look for companies that fulfil the quality criteria while being fairly priced.

Key terms

M-cap
Stands for market capitalisation. Obtained by multiplying the stock price by the total number of shares. Shows a company's market value or size.

Price to earnings (P/E)
The price-to-earnings ratio is simply the ratio of the price of a stock to its earnings per share. It shows in multiples how much investors are willing to pay for the earnings. High growth companies are assumed to have higher P/E's while low growth companies have relatively lower P/E.

Price-earnings to growth ratio (PEG)
Ratio of price to earnings to the EPS (earnings per share) growth of a stock. Demonstrates how high a price we are paying for the growth that we are purchasing. In all our analyses, we have taken five-year historic EPS growth.

Altman Z-score
Developed by Edward Altman of New York University, the Z-Score predicts a company's financial distress or the possibility of its going bankrupt within two years. A Z-Score of more than three is desirable.

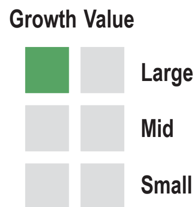
Piotroski F-score
Developed by Joseph Piotroski, the F-Score highlights financial performance as compared to that in the previous year. It thus points out the current outperformer in terms of profitability and financial improvement. An F-Score of seven or above is good.

Stock rating
Value Research Stock Rating combines the three scores (quality, growth and valuation) based on assigned weights to arrive at a holistic stock rating. We have created a five-star rating system. The higher the stock rating, the better.

Return on equity (ROE)
Measured by taking profit after tax as a percentage of the net worth of the company. Indicates how efficiently the company has been able to utilise investors' money.

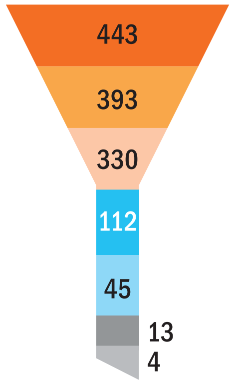
EPS growth (%)
The three-year annualised growth rate of a company's earnings per share (EPS).

Stock Style
Derived from a combination of the stock's valuation – growth or value – and its market capitalisation – large, mid and small. For example, here is the stock style of a largecap growth stock.



Attractive blue chips

No. of companies that cleared the filters



Reasons to invest

- Liquidity
- Large companies in respective businesses
- Strong balance sheets
- Liked by institutions

The filters

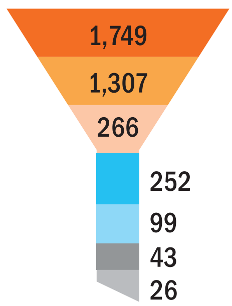
- Market cap greater than ₹12,572 crore
- D/E 0 to 2
- Interest coverage ratio more than 2
- ROE 5Y avg more than 20 per cent
- EPS 5Y growth more than 20 per cent
- PEG (5Y) 0 to 1.5
- 5Y ROE consistency without losing 20 per cent YoY

Company Industry	Stock style	Stock Rating	P/E	PEG	Debt-equity ratio	5Y avg RoE (%)	5Y EPS growth (% pa)	Market cap (₹ cr)	Share price (₹)	52-week high/low (₹)
Hindustan Aeronautics Defence & Aerospace Div.		★★★★	42.6	1.09	0.0	24.7	26.5	3,24,610	4,868	5,675-1,768
Persistent Systems Software & Services Div.		★★★★	60.8	1.25	0.0	21.5	28.2	71,194	4,580	4,929-2,317
Angel One Brokerage Services		Unrated	15.8	0.42	0.4	32.2	48.1	18,909	2,105	3,896-1,452
E.I.D. Parry Diversified Chemicals		★★★★	15.2	0.37	0.2	26.0	42.3	13,658	768	833-453

Data as of July 19, 2024

Quality stocks available cheap

No. of companies that cleared the filters



Reasons to invest

- Safety
- Soundness
- Good performance
- Reasonable valuations

The filters

- Market cap more than ₹500 crore
- Z-score greater than 2.99
- F-score greater than 7
- C-score less than 4
- Earnings yield more than 5 per cent
- PEG ratio between 0 to 1
- P/E to median P/E less than 1.5 times

Company Industry	Stock style	Stock Rating	Altman Z-Score	Piotroski F-Score	Modified C-Score	Earnings yield (%)	P/E to median P/E	Market cap (₹ cr)	Share price (₹)	52-week high/low (₹)
Jindal Saw Iron & Steel		★★★	3.2	9	1	12.0	1.0	17,188	538	598-300
Tanla Platforms Satellite Service Operators		★★★★★	18.9	8	2	5.2	0.8	13,217	971	1,318-782
JK Paper Paper & Paper Products		★★★★★	3.4	9	1	13.2	1.5	9,927	564	639-312

STOCK SCREEN

Company Industry	Stock style	Stock Rating	Altman Z-Score	Piotroski F-Score	Modified C-Score	Earnings yield (%)	P/E to median P/E	Market cap (₹ cr)	Share price (₹)	52-week high/low (₹)
Maharashtra Seamless Steel Tubes & Pipes		★★★★★	8.0	8	1	15.3	0.9	8,611	642	1,097-465
AGI Greenpac Containers & Packaging - Div.		★★★	4.0	8	0	7.8	1.3	5,040	776	1,089-575
WPIL Pumps & Compressors		★★★★	4.1	8	0	7.1	0.9	4,401	453	4,944-430
Nucleus Software Software		★★★★★	9.7	8	0	5.5	1.2	4,127	1,504	1,823-945
Indian Metals & Ferro Diversified Mining		★★★★★	6.3	9	1	14.6	1.2	3,786	707	880-329
Vadilal Industries Dairy Products		★★★★	6.9	8	2	6.1	1.2	3,068	4,237	5,143-2,133
Kingfa Science & Tech Commodity Chemicals - Div.		★★★★	6.0	8	2	5.6	0.7	3,042	2,498	2,856-1,509
Andhra Paper Paper & Paper Products		★★★★★	4.7	9	1	30.6	1.1	2,249	571	675-407
Taj GVK Hotels Hotels & Resorts		★★★★	10.1	9	2	5.8	0.7	1,987	317	423-213
Bharat Wire Ropes Steel Wires		★★★	7.1	8	1	7.9	0.8	1,663	243	401-192
Kuantum Papers Paper & Paper Products		★★★★	3.4	8	1	15.2	1.0	1,425	161	226-126
Satia Industries Paper & Paper Products		★★★★★	3.9	8	1	17.0	0.6	1,269	127	155-100
The Sandesh Advertising & Marketing - Div.		★★★★★	26.9	8	0	32.0	1.0	1,184	1,548	1,777-938
Chaman Lal Setia Exports Crop Farming		★★★	7.3	8	1	14.2	1.2	1,081	209	270-174
Royal Orchid Hotels Hotels & Resorts		★★★★	7.2	9	0	7.9	1.2	955	342	449-280
Tribhovandas Bhimji Zaveri Gems & Jewellery		★★	3.2	9	2	8.8	1.2	947	139	154-84
Linc Stationery & Office Supplies		★★★★	9.0	9	0	5.4	0.9	891	602	900-463
UP Hotels Hotels & Resorts		★★★★★	35.9	8	1	5.2	1.2	837	1,549	1,999-590
S Chand And Co. Book Publishing		★★★	6.9	8	1	9.0	0.6	808	229	335-187
Speciality Restaurants Restaurants & Bars		★★★★★	8.1	8	0	7.7	1.1	805	167	287-153
Nitta Gelatin India Commodity Chemicals - Div.		★★★★★	9.8	8	2	16.3	0.8	726	804	1,184-711

Data as of July 19, 2024. For the full list, scan the QR code on the right.

Want more? Here you go

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High Growth Large Caps

Gives you large caps that are still consistently growing at a brisk rate

	P/E		P/E
Tata Motors	10.6	Havells	80.1
Adani Power	12.8	Siemens	105.6
Sun Pharma	39.6	ABB India	110.7
Lupin	42.7	Trent	123.7
Cummins	57.9	Avenue Supermarts	123.7

Growth at Reasonable PE

Gives a list of growing stocks at cheap valuations

	P/E		P/E
Ind-Swift Labs	1.9	Albert David	9.3
Vipul	2.4	Wanbury	11.0
Ashima	8.4	Arihant Capital	11.8
Zuari Agro Chemicals	8.8	Kriti Nutrients	12.6
Saraswati Commercial	9.0	Radhika Jeweltech	13.9

5-star Stocks

Gives you a list of companies that have received a five-star Stock Rating

	P/E		P/E
Shreyans Industries	4.6	Albert David	9.3
Star Paper Mills	6.2	Jenburkt Pharma	14.7
Swadeshi Polytex	6.6	Alufluoride	21.4
Oriental Carbon & Chem.	8.2	Multibase India	28.0
Manaksia	8.4	Chemcrux Enterprises	41.0

Small Cap Growth

Gives a list of small-cap companies that are growing aggressively

	P/E		P/E
Kama Holdings	10.1	H.G. Infra Engineering	20.5
IIFL Securities	11.1	Man InfraConstruction	23.8
Share India Securities	14.4	Route Mobile	30.2
Banco Products	17.9	Gravita India	38.7
Shriram Pistons & Rings	18.7	Tips Industries	55.7

Book Value Discount

Gives you potential bargains that are trading below their book values

	P/B		P/B
Dhunseri Investments	0.3	The South Indian Bank	0.8
Jindal Poly Inv. and Finance	0.4	The Karnataka Bank	0.8
Dhunseri Ventures	0.4	DCB Bank	0.9
Zuari Agro Chemicals	0.5	Bank Of India	0.9
RSWM	0.8	Tamil Nadu Newsprint	0.9

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- Stock Rating
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www.valueresearchonline.com/stocks-screener/

Chandra Shekhar Ghosh, CEO, Bandhan Bank

On the requirement for more control as the industry scales up

You cannot manage 30 million customers in a bank today in the same manner as I did with 5 million customers 10 years ago. Scaling up involves relying on a large number of people and layers. When you are small, you can be directly involved, but as you grow the business, it becomes essential to have well-established compliance and risk mitigation processes and systems in place. Without these, the business's future growth will be impacted.

Business Today, June 23, 2024

Ipsita Dasgupta, Managing Director, HP India

On how HP will combat declining PC sales

But let's just talk about gaming for a second… there are 300 million gamers in India already. Still, only a single-digit percentage of gamers is on PCs. However, if you look at the way gaming is moving - as a country, we're getting into e-sports and gaming competitions - we are using gaming as a way to generate income. Automatically, you move towards the PC when you think about gaming in those ways.

Business Today, July 21, 2024

Sanjeev Bikhchandani, CEO, Info Edge

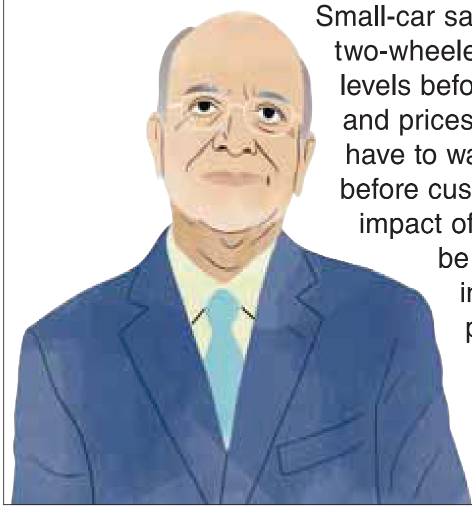
On the current funding winter in the start-up ecosystem

If the company's business is on the right path, funds will always be available, and anyway, to raise funds despite winter, you must fix the flaws within the company. Of course, we can say that there is a shift from the earlier scenario of funding where probing questions were not being asked enough, and GMV (gross merchandise value) was being valued over cash flow and profits; however, now investors are asking the right kind of questions.

Outlook Business, May 2024

RC Bhargava, Chairman, Maruti Suzuki

On the falling demand for smaller cars in India



Small-car sales will revive after the two-wheeler volumes reclaim their levels before BSVI came into force and prices went up. I guess we have to wait at least till late 2026 before customers are back, as the impact of these high prices will be absorbed by the increase in the purchasing power of people in that category.

Business Today, July 7, 2024